

# NASD News

PUBLISHED BY THE NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Volume VI

Philadelphia, May, 1945

Number 1

## New Registration Amendments and Some Suggestions

Members of the NASD can comply with new requirements of the Securities and Exchange Commission to furnish additional information respecting certain "Items" in broker-dealer applications (including data on salesmen and other employees) by using the standard 6-M Form (for supplemental statements) supplied by the Commission. Registrants have until July 9 to file the amendments.

The following alternative suggestions are offered NASD members in connection with their filings to comply with the new requirements:

1. Compare Items 5, 7, 15, 16, 18, 19, 20, 21 and 22 of your original application and the supplemental statements filed by you to date with the amended Items set forth in Securities Exchange Act Release No. 3674 (This presumes that you have copies of the application and all supplemental statements in your files.) If you find on such comparison that any amended Item requires more information, or a different answer from that on file already, or if any amended Item requires no additional information or different answer, prepare answers on separate paper, listing  
(Continued on page 4)

## 7th War Loan Drive Again First Job of Securities Firms

Just as each of its predecessors has been, the Seventh War Loan Drive now under way is the first order of business for securities dealers.

From May 14 to June 30, and particularly during the whole of June, sales forces of the business, organized as members of teams or working as individuals and groups, will concentrate their energies on the package of securities being offered in the present drive. These consist of four issues of marketable securities as well as the traditional Series E, F and G savings bonds and Treasury savings notes.

Dated June 1, 1945, marketable securities to be issued in the drive follow: 2½'s maturing June 15, 1972, redeemable on and after June 15, 1967; 2¼'s maturing June 15, 1962, redeemable on and after June 15, 1959; 1½'s maturing December 15, 1950, and 7/8's indebtedness certificates maturing June 1, 1946.

Underwritings of new corporate issues of securities will be kept to the absolute minimum during the period May 14 to 30, and during June none will come on the market the offering of which can be delayed beyond the closing date of the drive.

## Dangers of Laxity of Control Over Employees Shown in SEC Decisions

The dangers of lax or ineffective supervision of key employees—salesmen, traders or others having authority to commit firms to transactions or courses of action—are forcefully demonstrated in several SEC decisions in recent months. One decision revoked the SEC registration of the firm involved and in four other instances suspensions of NASD memberships of from 10 days to two months were imposed. In each case, aside from the direct penalty incurred during a lapse of NASD membership, more or less general publicity attended release of the Commission's decisions.

Commission attitude on the matter of responsibility of partners, officers or sole proprietors for acts of employees is revealed in the following passage from one of the decisions:

... where a broker-dealer firm has a substantial number of employees, where considerable authority is delegated and where subordinates have power to exercise wide discretion, the protection of investors can obviously not be achieved if the firm is permitted to shield itself from the consequences of a subordinate's undetected violations by pleading the very conditions which made the violations possible. It cannot therefore be allowed to point to the officers' ignorance of the actual violations to insulate itself from the consequences of such actions. With responsibility imposed by statute upon the firm, and with business prudence, in addition, requiring the exercise of supervision, . . . (disavowals) of fraud committed by a subordinate can all too readily lead to a firm's enjoying the fruits of wrongful conduct while avoiding the statutory consequences when such conduct is discovered."

Willful violations of the Securities Exchange Act were found against the firms despite the Commission's acknowledgments that in one degree or another the violations occurred perhaps without knowledge of partners or officers. In one instance the Commission conceded that "relative inefficiency" was, in part at least, "due to the war."

The securities business has labored hard to meet personnel problems growing out of the war. Responsible heads of a firm have nevertheless to maintain exacting vigilance over the conduct of the firm's affairs to safeguard against excessive exercise of authority on the part of employees to whom authority may have been delegated.

Respecting effect on a member of suspension from NASD, see article on page 3 reviewing this subject.

(Reprinted by Permission)

# MONEY AND COMMERCE

PITTSBURGH, PA., FEBRUARY 24, 1945

## NASD PROTECTS INVESTORS

After serving two and one-half years on the Board of Governors of National Association of Securities Dealers, Inc., I feel justified in using the above caption. The Association is registered with the Securities and Exchange Commission as a National Securities Association pursuant to section 15A of the Securities Exchange Act of 1934, as amended. The certificate of incorporation clearly states the purpose of the Association (1) to promote high standards of commercial honor, and (2) to adopt and enforce rules of fair practice and rules to prevent fraudulent practices, and in general to promote just and equitable principles of trade for the protection of investors.

To effectuate these purposes, Rules of Fair Practice were adopted in 1939, and have been administered since that time. The following is a summary of requirements and activities that contribute to the protection of investors:

1. Practically all dealers and brokers active in the distribution of corporation bonds and stocks are members of NASD, and thus are subject to investigation and discipline. On December 31, 1944, there were 2,214 member firms in the U. S. A.
2. Sufficient records must be kept and made available for inspection at any time.
3. Confirmation forms must accurately indicate the relationship between member firm and customer.
4. The price at which a member firm, acting as principal, sells securities to the public shall be reasonably related to the market for such security

By S. K. CUNNINGHAM,  
President, S. K. Cunningham & Co., Inc.,  
Pittsburgh.

Mr. Cunningham, former Chairman of Western Pennsylvania Group, Investment Bankers Association of America, recently completed a three-year term as member of Board of Governors of the National Association of Securities Dealers, Inc.

at the time of sale, if there is an active or public market.

5. In the case of securities that have no public market, or a very inactive market, restrictions are placed on the profit margin of the member firm, which in substance require that said profit shall be fair and reasonable in the light of all the circumstances.
6. All member firms are required to fill in questionnaires from time to time, showing a detailed record of their transactions with customers. These questionnaires are examined by District Committees, and complaints filed and hearings held where the facts seem to justify such action.
7. The District Committees have authority to censure member firms, to impose fines within certain limits, to suspend from membership for a definite period of time and/or to expel from membership. Any action by District Committees may be appealed to the Board of Governors, whose decision in turn may be ap-

pealed to the Securities and Exchange Commission.

8. The supervision and disciplinary action so far have been very effective in promoting uniformity in practice, and in preventing unfair practices.
9. The entire program of NASD is based on the principle of self-regulation and self-discipline. We believe the standards of business ethics in the business are as high as in any other business or profession. It is the purpose of NASD to keep them high and to seek improvement.
10. Investors doing business with an NASD member firm are protected by the above regulations and control, in a way similar to the protection afforded to bank depositors and insurance policy holders by banking and insurance department laws and regulations. All member firms of NASD are authorized to make public the fact of their membership, and investors can readily ascertain whether or not a certain dealer is a member.

The above is submitted as general information, with the hope that it will contribute to a wider knowledge of the function and service rendered by the National Association of Securities Dealers, Inc. It is the desire of all reputable dealers and brokers that investors shall have proper protection. It is the function of NASD to provide this protection. Co-operation of investors will help in making the protection more effective.

**(b) Over-the-Counter Trading**

An Association member may not pay a commission to any non-member broker or dealer for executing a brokerage order for the Association member in the over-the-counter market. Rule 25 requires an Association member to deal with non-members only on the same terms and conditions as are accorded by such Association member to members of the general public. On the other hand, Rule 25 does not prohibit an Association member from executing over-the-counter an order for a non-member and charging such non-member a commission therefor. Rule 25 merely requires that in transactions with a non-member, such non-member must be dealt with 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.

In over-the-counter transactions in either listed or unlisted securities an Association member may not buy from or sell to a member of a national securities exchange who is not also a member of the Association at different prices or on different terms or conditions than are accorded by such Association member or members of the general public. Such exchange member, with respect to such over-the-counter transactions, comes within the definition of a "non-member broker or dealer" in Rule 25 (d), and Rule 25 is therefore applicable. For the same reason an Association member may not pay a commission to an exchange member, who is not also a member of the Association, for executing a brokerage order over-the-counter.

When a dealer has been and is suspended or expelled from membership in the Association by order of the Securities and Exchange Commission or of the Association, under Rule 25, during the period of such suspension or expulsion, an Association member may only deal with such dealer at the same prices, for the same commissions, fees, concessions, discounts or other allowances as the Association member would deal at the time of the transaction with a member of the general public.

**Board, District Chairmen to Meet June 4-5**

The regular Spring meeting of the Board of Governors and Advisory Council will be held June 4 and 5 at Seaview Country Club, Absecon, N. J. The Advisory Council consists of the fourteen District Chairmen.

Governors of the Association who will attend the meeting follow:

Ralph E. Phillips, Chairman; Peter Ball, William K. Barclay, Jr., Harry W. Beebe, Ralph Chapman, Hermann F. Clarke, R. Winfield Ellis, Irving D. Fish, Firmin D. Fusz, Jr., J. Wesley Hickman, June S. Jones, Robert S. Morris, Norman Nelson, James Parker Nolan, B. Winthrop Pizzini, John J. Quail, Henry G. Riter, 3rd, John B. Shober, J. Robert Shuman, Burdick Simons.

District Chairmen who will attend the meeting follow:

Fred M. Blankenship, Eaton Taylor, Joseph L. Ryons, Ralph G. Bulkley, Guy M. Phillips, Earl W. Price, W. Rex Cromwell, Roy A. Dickie, Sampson Rogers, Jr., Clement A. Evans, Edward E. Parsons, Jr., Robert C. Kirchofer, S. Davidson Herron, Edward Boyd, Jr., George N. Lindsay, T. Jerrold Bryce, B. Earle Appleton.

**New Registration Amendments . . . .**

*(Continued from page 1)*

each Item by number, and attach to Form 6-M. Under Section "B" of Form 6-M you should state that the information supplied in the exhibits attached is filed pursuant to Rule X-15B-2 and Form 3-M, as amended and described in Securities Exchange Act Release No. 3674. File two complete signed copies with the Securities and Exchange Commission, Philadelphia.

2. Furnish complete answers (even if "No Change" is the answer) to Items 5, 7, 15, 16, 18, 19, 20, 21 and 22 as set forth in Securities Exchange Act Release No. 3674. Prepare answers on separate paper, listing each Item by number, and attach to Form 6-M. Under Section B of that form you should state that the information supplied in the exhibits attached is filed pursuant to Rule X-15B-2 and Form 3-M, as amended and described in Securities Exchange Act Release No. 3674. File two complete signed copies with the Securities and Exchange Commission, Philadelphia.

3. If you have not kept in your files copies of your original application and all supplemental statements filed to date, file a complete amended application on a new Form 3-M now available. In such event, write or type the words "Amended Application" at the top of page 1 of Form 3-M. Answer all Items anew. File two complete signed copies with the Securities and Exchange Commission, Philadelphia.

Any one of the above methods would satisfy the requirements whether you filed originally on Form 1-M, 3-M or 4-M.

The amendments and the new form do not require a listing of all salesmen or other employees. Only certain salesmen or other employees must be listed and information concerning them supplied. For example, information concerning a salesman or other employee is required:

Under Item 21 only if such salesman or other employee is under injunction involving securities transactions.

Under Item 20 only if such salesman or other employee was convicted within the past 10 years of any felony or misdemeanor involving securities transactions.

Under Item 19 (a) only if such salesman or other employee, during the past 10 years, held a managerial position (partner, officer, director, trustee, branch office manager, controlling person, etc.) with any broker or dealer which, during the period of such connection, was the subject of any of the actions or proceedings enumerated in clauses 1 to 5 of this Item.

**Barclay Elected Treasurer**

William K. Barclay, Jr., partner of Stein Bros. & Boyce, Philadelphia, has been elected Treasurer of the National Association of Securities Dealers, Inc., to succeed John H. Barret, Stern Brothers & Co., Kansas City, Mo. Mr. Barclay will also serve on the Executive and Finance Committees of the Association. Mr. Barret resigned as Secretary of Stern Brothers to devote full time to personal business affairs.

Mr. Barret's term as a Governor expires January 13, 1946. A successor to the vacancy on the Board of Governors will be elected by the members of District No. 3 through the established election machinery.

## EFFECT OF SUSPENSION OF NASD MEMBERSHIP

The Association has received numerous questions relating to the manner in which the Rules of Fair Practice may affect transactions between members and non-members of the Association. The Association rules are binding only upon Association members but affect non-members indirectly in transactions with members. The answers to many questions relating to the applicability of the rules to a particular transaction will depend upon the circumstances in the particular case. The discussion in this article is, therefore, limited to general situations which may arise and considers (1) persons who are members and who are non-members of the Association, and (2) over-the-counter transactions which are divided into separate considerations of (a) participation in underwriting and selling groups and (b) over-the-counter trading.

### 1. Non-Members of the Association Under the Rules of Fair Practice

Section 1(c) of Article II of the Rules defines a "member" as any individual, partnership, corporation or other legal entity admitted to membership in the Association. All other persons, firms or corporations, whether or not they are brokers or dealers, are therefore to be regarded as non-members of the Association.

A dealer who has been *expelled* from the Association by order either of the Securities and Exchange Commission or of the Association becomes a non member of the Association from the effective date of such order.

A dealer who has been *suspended* from membership in the Association by order either of the Securities and Exchange Commission or of the Association is to be treated as a non-member of the Association from the effective date of such order and during the period of such suspension. At the termination of the suspension period, such dealer is automatically reinstated to membership in the Association.

Revocation by the Securities and Exchange Commission of an Association member's registration as a broker or dealer automatically terminates the membership of such broker or dealer in the Association as of the effective date of such order.

### 2. (a) Participation in Underwriting or Selling Groups

An Association member may not enter into a joint account, underwriting or selling group, or join a syndicate or group, with any non-member broker or dealer or with a member of a national securities exchange, who is not also a member of the Association, for the purpose of acquiring and distributing an issue of securities. (Rules 25(a) and 25(b).)

An Association member may not join any underwriting or selling group with a dealer who has been and is suspended from membership in the Association by order of the Securities and Exchange Commission or of the Association if, at the time such group was organized, it was contemplating the distribution of an issue of securities to the public. A dealer who has been suspended from mem-

bership in the Association is to be treated as a non-member during the suspension period and Rule 25(b) (2) prohibits members from joining with non-members in a group "contemplating the distribution to the public of any issue of securities." Even though the suspension period had terminated before the time when the securities were to be distributed, the rule prohibits a member from joining with a non-member in a group which is contemplating the distribution of an issue of securities at a future time.

Where a dealer is suspended or expelled from membership in the Association by an order of the Securities and Exchange Commission or of the Association which became effective after such dealer had joined an underwriting group under which each underwriter had severally purchased securities from the issuer, such dealer could thereafter during the period of suspension or expulsion, accept delivery from the issuer of the securities which it had underwritten prior to the effective date of such order and pay to the issuer its commitment therefor, without involving any violation of the rules. After the effective date of such order and during the period of suspension or expulsion, Association members could only buy the securities from or sell the securities to the dealer, who was suspended or expelled, at the public offering price, regardless of whether the Association members were also members of the underwriting or selling group for the particular issue. Rule 25 prohibits an Association member from dealing with any non-member broker or dealer except at the same prices, for the same commissions or fees, and on the same terms and conditions as the member would deal with a member of the general public at the same time. Delivery of the securities by the issuer to the particular dealer suspended or expelled and payment therefor by such dealer would not involve a violation of Rule 25 in this situation.

Where a dealer is suspended or expelled from the Association by an order of the Securities and Exchange Commission or of the Association which became effective after such dealer had joined a selling group, members of the Association, including the underwriters and other selling group members, would be prohibited by Rule 25 from selling the securities to, or buying the securities from, such dealer at any price different from the public offering price. Members would not violate Rule 25 by accepting from such dealer, during the period such order of suspension or expulsion was in effect, payment of the full public offering price for the securities allotted to such dealer. After the effective date of such order Rule 25 prohibits Association members from granting or allowing to the dealer suspended or expelled any selling concession, discount or other allowance for the securities distributed by such dealer. While such order is in effect, Association members could only deal with such dealer at the same prices, for the same commissions, fees, concessions, discounts or other allowances as the Association members would deal at the time of the transaction with a member of the general public.

(Continued on next page)

## Report on Salesmen Part of Statistical Program

Vital statistics on the investment banking and securities business, particularly the over-the-counter branch of the business, have never been gathered on a scale and with a continuity comparable to programs of this kind carried on by practically every major line of business activity in the country. As a result, the investment banking and securities business has not always been as well fortified with facts and figures in support of its position at times when such facts and figures could have been employed to good advantage. The Board of Governors of NASD has from the start of the Association been aware of deficiencies in this field. It has endeavored from time to time to correct the situation and hopes that as time goes on more and more constructive and useful information to protect and promote the welfare of the business can be gathered and accumulated with that end in view.

One step in this direction was taken several weeks ago through the means of a form sent to all members requesting information about the number of salesmen employed, and general information concerning method of compensation. This was the first such inquiry to be made by the Association and, for this reason, a number of members asked as to its purpose—pointing out that compensation arrangements were private matters, not the property of competitors. It, perhaps, had not been made clear that the report on salesmen and other "producers" of a firm would not be published nor the privacy of the information violated insofar as the individual member is concerned. Primarily, this inquiry was a part of studies being made of a number of fundamental characteristics of the business. Statistics to be compiled from the reports filed will be studied and their general import conveyed to the Board of Governors. As with other questionnaires filed by members in the past several years, the reports on salesmen are received, analyzed and filed in the Executive Office—for all material of this kind is considered of confidential nature, unless Rules of Fair Practice of the Association appear to have been violated or jeopardized.

## Securities Commissions Act Against Toronto Soliciting

Securities Commissions of the various states have for some time been faced with the problem of solicitations by companies and persons in Toronto, Canada, for the sale of mining stocks and other similar types of securities to residents in this country. Such solicitations have involved violations of securities laws of the United States and the various states.

State securities commissions, encouraged by announcements by the National Association of Securities Commissioners, have been issuing cease and desist orders against many of the organizations in Toronto that have been soliciting securities' business in the United States.

Members of NASD can co-operate with their State Commission by advising it of activities of this kind which come to their attention. Meanwhile, the Association itself is engaged in various endeavors aimed at correcting these conditions.

## Pennsylvania Commission Clarifies Requirements on New Offerings

The Pennsylvania Securities Commission has issued a statement clarifying the section of the Securities Act having to do with filings of underwriters and dealers in the state in connection with offerings of securities. The effect of the clarification is to make it permissible for the registered underwriter or syndicate manager to file a prospectus containing names of participants in the underwriting and to supplement this filing with additional names of Pennsylvania dealers subsequent to the day of offering.

This co-operative action on the part of the Pennsylvania Commission followed discussion of the matter at a meeting in Philadelphia of members of the Commission and representatives of NASD—William K. Barclay, Jr., Governor, District No. 12, and Wallace H. Fulton, Executive Director. It was pointed out at the meeting that Pennsylvania's requirements in respect to new offerings were perhaps not clearly understood; that in view of present personnel conditions and the quantity of new offerings in prospect, prevailing misunderstanding of the Commission's rules might be removed by a clarifying statement. In its April 1st Bi-Monthly Bulletin, the Commission said:

"There appears to be a misunderstanding of the requirements for filing prospecti in accordance with Section 13 (2) of the Act, the first sentence of which reads:

'No dealer or salesman shall issue or publish in this state any analysis or prospectus until such dealer shall have been registered or temporary permission shall have been obtained as in this Act provided.'

"The misinterpretation has arisen from the following sentence occurring later in the same Section:

'No dealer or salesman shall issue or publish in this state any prospectus unless a copy thereof in which or on which a list attached to which the dealer's name appears as a proposed vendor, shall have been filed in the office of the Commission or mailed to the Commission in Harrisburg, Pennsylvania, by prepaid registered mail.'

"This provision was incorporated in the 1939 Act and included in the present Act of 1941. Prior acts required a true copy of each prospectus be filed by each dealer using it. The present requirement permits the registered underwriter or registered representative of the syndicate to file a prospectus furnishing lists of participants in the distribution of the issue which, in turn, obviates the necessity for each registered dealer to file in his own behalf. Realizing that last-minute additions to the distributing group may occur after the information as to such participants has been mailed to the Commission, the Commission has been accepting additional lists supplementing the original filing."

The Pennsylvania Securities Commissioners are: R. A. Cox, Chairman, and J. Myron Honigman, Secretary of the Commission is I. G. Myers.

## Membership Certificates for 1945

All members of the Association are entitled to a Membership Certificate, which may be displayed in their offices. Write to the Executive Office if you wish to have one.

### 1945 Examination Program Is Under Way; All Members to Be Covered in Few Months

The Association's questionnaire examination of members in 1945 got under way the middle of April with the mailing from the Executive Office in Philadelphia of the first of the forms to be used by members in supplying the required information. Periodically, over the next several months, additional questionnaires will be mailed until all members have been covered. The Board of Governors at its meeting in January, after considering experience and results of questionnaire examinations in 1944 and 1943, favored continuation of the program in the current year. At a subsequent meeting, District Chairmen and District Secretaries discussed the 1945 program in detail and approved the procedure to be followed.

Instead of 50 consecutive principal transactions on which pricing information was obtained in 1944 and 1943, members are being asked this year to report on a maximum of 75 transactions, agency as well as principal. To obtain a more representative picture of a member's business over a longer period of time than in the past two years, the 75 transactions to be reported on are to be comprised of the first 25 transactions in each of three months specified in the instructions going to members. A separate schedule is provided for each of the three months.

Members are also being called upon this year to supply completed sample confirmations on certain types of transactions. The schedules and confirmations will be accorded the same confidential treatment as questionnaires filed in past years, which means that unless an apparent cause for action exists, identity of the member is not divulged to District Committees which examine the questionnaires.

As pointed out in the letter transmitting the schedules and forms, Governors of the Association who pass on policy respecting examination programs, and District Chairmen of the Association who examine and pass on these programs in detail, are all engaged in the securities business and are familiar with its current personnel and related problems. Every effort was made to simplify the examination to be made this year commensurate with the necessity of obtaining precise and material information on the practices with which the questionnaires are concerned.

### Caffrey New Commissioner

Nominated by the late President Roosevelt and confirmed by the Senate April 25, James J. Caffrey, former New York regional administrator of the Securities and Exchange Commission, has succeeded Robert H. O'Brien on the Commission for a term expiring June, 1950. Other Commissioners are: Ganson Purcell, Chairman; Robert E. Healy, Sumner Pike and Robert K. McConnaughey.

Mr. Caffrey is 47. He is a graduate of Harvard Law School, practiced law in Boston and first entered Government service with the Reconstruction Finance Corporation. As regional administrator in New York, he has been in charge of the largest and most important financial and securities area of the country. During World War I he served as a Lieutenant in the Marine Corps.

### Relief on Transfer Tax Obtained in New York

Effective July 1, the New York State transfer tax on stocks selling below \$5 a share will be 1 cent per share instead of 3 cents, and on stocks selling at \$5 and less than \$10, 2 cents a share instead of 3 cents. Prevailing total of 3 cents on stocks selling at \$10 and less than \$20, and of 4 cents on stocks selling at \$20 a share and over remain in effect.

On transfers not connected with a sale the tax will be 2 cents a share.

### Change in "Red Herring" Policy

In a "general policy" statement issued April 30, the SEC said that it will not order acceleration of the effective date of a registration statement in a case where a "red herring" prospectus was inaccurate or inadequate in material respects until the Commission "has received satisfactory assurances that by appropriate means the nature of the material amendments to the registration statement have been communicated to those persons to whom the 'red herring' prospectus was distributed."

### New York Member Meeting

George N. Lindsay, Chairman, District Committee No. 13 (New York, New Jersey and Connecticut), announces that a general meeting of members will be held in New York City the afternoon of June 8. Time and place will be made known to members in the area as soon as arrangements have been completed.

Mr. Lindsay's announcement states that Ralph E. Phillips, Chairman of the Board of Governors of NASD, will discuss activities of the Association, after which the meeting will be thrown open to discussion of questions to be submitted by members in attendance.

### Hickman Is Texas Choice

J. Wesley Hickman, Schneider, Bernet & Hickman, Dallas, Texas, has been elected to the Board of Governors representing District No. 6 (Texas). Mr. Hickman succeeds Mr. P. B. Garrett.

### NASD NEWS

Published periodically by National Association of Securities Dealers, Inc., under the supervision of the Public Relations Committee:

Henry G. Riter, 3rd, <i>Chairman</i>	James Coggeshall, Jr.
James Parker Nolan	Francis F. Patton
Ralph E. Phillips	Wallace H. Fulton

James P. Conway, *Editor*

Salesmen, traders, cashiers as well as partners and officers of members should read the NEWS.

For extra copies, supplied free of charge, write Wallace H. Fulton, Executive Director, 1616 Walnut St., Philadelphia 3, Pa.