Law School of Harvard University

Cambridge 38, Mass.

1963 Leg
General

April 25, 1963

The Honorable
William L. Cary
Chairman
Securities and Exchange Commission
Washington 25, D. C.

Dear Bill:

My comments on the five sets of legislative proposals you sent me will be relatively sparse. I don't know whether that is a reflection of your wisdom at the SEC or my lack of imagination or both. To some extent, I am sure, it reflects the fact that I have not had the advantage of chewing these proposals over around a table -- though, of course, some of them are fairly "old hat." Moreover, I should make it plain that I have not reviewed the actual language as I would if I had the ultimate responsibility for it. Every legislative draftsman has his own style. This language is not in my style for the most part. I don't say that critically. It is simply a fact.

On the merits, I have no quarrel with any of the proposals. They should be all to the good. Each additional excrescence, of course, does emphasize the need for a general codification. But you know my views on that. And I agree that that is food for another day.

Now that I have probably spent more time on the introduction than on the guts of this letter, let me proceed to the few comments that I have:

(1) The language of the proposed amendment to §4(1) of the 1933 Act would do less violence to the present language and would also be considerably shorter, it seems to me, if the underscored words

immediately preceding the new clause (c) were deleted and the new sentence at the end were changed to read: "With respect to transactions in subparagraph (b), the applicable period shall be ninety days instead of forty days if the issuer has not previously had an effective registration statement. The Commission may shorten either period by rules and regulations or by order."

(2) The proposed §10(c) of the 1934 Act, with respect to corporate publicity and public relations, is the proposal which, it seems to me, is most likely to raise a rumpus because of its breadth. I am sure you have considered this. But I can't help wondering whether it is worth the candle, particularly since I am not sure what it would enable you to do that you could not already do by adopting a statement of policy or an interpretative rule under §9(a)(2), which would carry over to the fraud provisions so far as non-listed securities are concerned. When I was Chief Counsel to the Trading Division back in 1944-48, we began to develop the concept that §9(a)(2) could be violated indirectly without effecting any transactions at all. See pages 1558-60 of my book. That is one development which has not matured over the years as other administrative developments have. Have you thoroughly considered whether that concept of indirect manipulation, particularly when buttressed by §20(b) and one or more statements of policy or interpretative rules, would not give you what you want with less danger to the "public relations" aspect of your entire legislative program? I must confess that the proposed §10(c) seems perhaps unduly broad to me. If so, I can only imagine how it might seem to others.

(3) If you do advance your §10(c) proposal, I am troubled by the last sentence of the supporting memorandum. It seems to me that a legislative body should either button up the civil liability question one way or the other or ignore it. I see no logical room for having the legislative history indicate

that the implication of liability by the courts is "probable." To put it differently, I rather fear that a sentence like this might lead the courts to refrain from implying a civil liability under this section on the ground that the legislative failure to make it express when the question was specifically brought to its attention indicates an intention not to have any such liability. Of course, as Dean Thayer put it in his classic essay back in 1914, the courts ought not to try to discover "supposed legislative intent" when the question of civil liability was not considered by the legislature one way or the other. It then becomes a matter of judicial construction to determine to what extent the particular statute should be used as a guideline in defining duties under the common law of torts. See page 935 of my book. The trouble is that, when the legislative history is not silent on the question, it becomes difficult for the courts to carry out this classic function. Consequently, I would either drop the last sentence of the memorandum or I would change it to read simply: "The question whether a violation of the Act or the rules thereunder should give rise to civil liability is left to the courts."

(4) So far as the "Frear-Fulbright" proposal is concerned -- and I consider it poetic justice that Senator Frear is now in the position of urging his own proposal on his former colleagues -- why not amend §7(e) in order to give registered securities the same status as those which are listed insofar as registration carries an advantage rather than additional regulation? See pages 51-52 of the 1950 Senate hearings for the language. I believe that language was also carried over into the later Fulbright Bills. First of all, this seems correct in principle. Secondly, it might possibly gain additional support for the proposal.

(5) Although, as I have indicated, I am refraining from essentially stylistic criticism, I did have to read the second sentence of proposed §12(g)(1) several times because of the clumsy effect

created by having the plural, "financial manuals," follow the singular, "each national securities association." The problem would be solved very simply by inserting the word "such" before "recognized financial manuals." Just read the sentence that way and you'll readily see what I mean.

(6) In proposed §12(g)(3) I would again insert "such" before "recognized financial manuals" in the last sentence. And I think the first sentence would read more clearly in the following form: "The provisions * * * shall apply as if the security of the class required to be registered * * *." The substitution of the definite for the indefinite article should be obvious or I have not made my point. And, since the greater includes the lesser, I see no reason to refer to a class "registered" when you already refer to a class "required to be registered."

(7) Since you are substantially rewriting §15(d) anyway, isn't it quite safe in the year 1963, both constitutionally and otherwise, to drop the "undertaking" nonsense and simply to make it a direct obligation of registrants under the 1933 Act to file reports? We thought so way back in 1941. See page 822 of my book. I would simply introduce §15(d) with the language: "The issuer under each registration statement hereafter filed pursuant to the Securities Act of 1933, as amended, shall file with the Commission * * *." I would then delete the language about the operative data of the undertaking. And I would delete the language: "The issuer shall file such supplementary and periodic information, documents and reports pursuant to such undertaking, except that." In other words, I would start the sentence with: "The duty to file * * *." The language I would delete just before that seems to me utterly redundant, especially with the undertaking technique gone, since the duty to file would flow from the first sentence until it was suspended by the sentence in question. Of course, if the undertaking technique is gone, §32 and perhaps other sections will have to be carefully examined and adjusted accordingly. For example, the words, "An undertaking required under," should be deleted from §15(c)(4).

(8) In proposed §12(b)(3) you have incorporated the confidential treatment language for material contracts from ¶(30) of Schedule A of the 1933 Act even though §24(b) of the 1934 Act already gives at least as much protection to registrants. If you were to require confidential treatment on a finding without more that disclosure would impair the value of the contract, it might be logical to do what you have done. But your proposed language, like ¶(30) of Schedule A, requires the Commission to find, before confidential treatment follows, both that disclosure would impair the value of the contract and that it would not be necessary for the protection of investors, whereas §24(b) provides for confidential treatment on just the latter of these two findings, in substance. If the "but" clause was inserted in §12(b)(3) just to give specific assurance to registrants under the 1934 Act, I suggest that a statement in your forwarding memorandum and ultimately in the legislative reports to the effect that §24(b) already goes further would do the trick without the danger of lousing up the 1934 Act by including within it two disparate provisions on confidential treatment.

(9) At page 8 of the statement with respect to §§15(a) and 15A, it is stated that the intrastate exemption from broker-dealer registration "presumably reflects constitutional doubts of 1934." I seriously question that statement. If there were constitutional doubts about using the mail power in intrastate situations, they would presumably have carried over to §15(c) of the 1934 Act as well as §§17(a) and 12(2) of the 1933 Act. I had always assumed that the intrastate exemptions in both statutes were motivated by policy rather than constitutional considerations. That is to say, in the absence of fraud, if Nevada did not want to protect its own citizens by requiring the registration of securities or broker-dealers even though the intrastate nature of the security offering or the broker-dealer's business made it perfectly feasible for Nevada to do so, why should the federal government intervene? I am not saying I agree with that philosophy. I am saying merely that I think

that is what the philosophy was in 1933 and 1934. And this impression was fortified by a conversation I had with Jim Landis some years ago at a meeting of the North American Securities Administrators in Vancouver, where I gave a talk about my current work in drafting what became the Uniform Securities Act. He said to me at lunch, "You know, we almost made your present job unnecessary in 1933 by preempting the field." When I asked him why they had not done so, he replied simply: "Because we happened to believe in federalism." (Incidentally, have you noticed that Nevada just adopted a truncated version of the Uniform Securities Act -- which leaves Delaware all alone out in left field?)

(10) In connection with the same proposal, the new §§3(a)(18) and 3(a)(21) would define "person associated with a broker or dealer" and "person associated with a member." Wouldn't it be simpler to use the terms "associate of a broker or dealer" and "associate of a member"?

(11) In the proposed amendment to §15(a) which is part of the same package, the (A) is missplaced as a matter of syntax. It should follow "broker or dealer" instead of "unless." And the semicolon before "and (B)" should be a comma.

(12) So far as the proposed <u>new</u> paragraph of §15(a) is concerned, why shouldn't the exemptions in the last sentence of that paragraph be statutory rather than referred to Commission rule? I think I know all the arguments in favor of the flexibility of the rule-making power. But, in the nature of things, I can't imagine any situation in which the indicated exemptions should not apply. How could you ever require a broker or dealer to be a member of an association if there were no associations? In short, here I think that the general rule-making power in §23 should suffice if it should turn out to be necessary to smooth the edges of the statutory exemptions.

(13) In the new §15A(b)(5), at the top of page 6 of the set of proposals I am now talking about, Clause (F) would read a good deal more clearly if all the language from "and any application or document supplemental thereto" to the end were put in parentheses. Otherwise one reads Clause (F) as if "any application or document supplemental thereto" were the object of "in accordance with" instead of the subject of "shall."

(14) On the quotations bureau proposal, the first sentence of §15B(b) refers to registration by filing "a statement." The last sentence of that section refers to "the application." Sections 6(a) and 15A(a), as well as proposed §15B(g), use the phrase, "registration statement." This is merely one example -- perhaps not too important in itself -- of the stylistic inconsistencies which one must always guard against. I realize that the 1933 and 1934 Acts are already internally inconsistent with respect to this terminology. But I think that inconsistency would be kept to a minimum if §15B consistently used the phrase, "registration statement," as do §§6(a) and 15A(a).

(15) I would rewrite §15B(f) as follows: "A quotations bureau may withdraw its registration statement, before or after its effective date, upon such terms * * *."

(16) The present §15A(k)(2) is clumsily arranged in that its subclauses are numbered rather than lettered, so that we have the monstrosity of a §15A(k)(2)(2). Since you are amending that section anyway, why not repair the clumsiness by changing the (1)-(5) to (A)-(E). Statutory citation would be much easier and more accurate if every draftsman could remember to use the standard progression of numbers and letters as did the draftsmen of the 1935 Act, for example, in §2(a)(8)(A)(1).

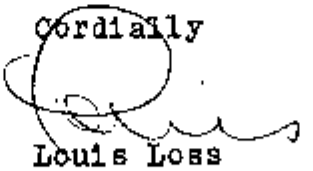
That's all the damage I can do for the moment. If I can be of any further help, don't hesitate to write or call. That includes coming down for a session around the table if you think it would be useful. I do have a couple of things pending before the staff -- one or two of which might just conceivably bring me to the table within the next few weeks. But they do not touch on any of the questions you have so far presented to me. And I had never supposed that a practicing lawyer was barred from discussing legislative or quasi-legislative proposals with an administrative agency on an uncompensated basis. Otherwise I don't see how bar committees could ever function unless they were made up of people who did not practice before the particular agency, in which event they would not be worth very much.

I would also be glad, if you thought it would help, to give evidence on the proposals before the appropriate legislative committees, as I did in 1954 at Ralph Demmler's request. But, in principle, I would not want to appear without an invitation from either the committee or the SEC.

I am sending a copy of this to Manny pursuant to his request.

With warm regards,

Cordially



Louis Loss

LL:m

P. S. I am slowly plowing through your report. Since the printed version will, of course, be differently paginated, I'd appreciate having a copy of that as soon as possible so that I shall not have to translate the original numbers to the final numbers when I annotate the report for my next supplement.