

[PUBLIC—No. 719—75TH CONGRESS]

[CHAPTER 677—3D SESSION]

[S. 3253]

AN ACT

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, to prevent acts and practices inconsistent with just and equitable principles of trade, 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, and 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 by such association or any member thereof 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 omission 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) by his conduct while employed by, acting for, or directly or indirectly controlling or controlled by, a broker or dealer, was a cause of any suspension, expulsion, or order of the character described in clause (A) or (B) which is in effect with respect to such broker or dealer;

"(5) the rules of the association assure a fair representation of its members 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 its members, 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, to provide safeguards against unreasonable profits or unreasonable rates of commissions or other charges, and, in general, to protect investors and the public interest, and to remove impediments to and perfect the mechanism of a free and open market; and are not designed to permit unfair discrimination between customers or issuers, or brokers or dealers, to fix minimum profits, to impose any schedule of

age, may become a member of such association, may be excluded pursuant to paragraph (1) of subsection (b). That the rules of the association in such association on such specified or on such specified basis relating to the conduct of its members, or on such other basis, as appears to the Commission to be in the public interest or for the purpose of carrying out the purpose of this section.

association provide that, except with the approval of the Commission in cases in which it is appropriate in the public interest, no broker or dealer shall be admitted to membership in such association, if (1) such person, prior or subsequent to becoming such, is a director, or branch manager of such association, or a person occupying a similar status or position, or any person directly or indirectly connected with such broker or dealer, whether before or after becoming such, (A) has been and is now a registered securities association (other than a national securities association) or from a national securities association, or (B) has violated any rule of such association or any act or transaction constituting a violation of just and equitable principles of trade, or (C) the Commission denying or revoking registration pursuant to section 15 of this title, or expelling membership in a registered securities exchange, or (C) by his conducting for, or directly or indirectly through, a broker or dealer, was a cause of, or order of the character described in section 15 of this title, or (D) is in effect with respect to such broker or dealer.

association assure a fair representation of the interests of its members, and the selection of its officers and directors, and the administration of its affairs:

association provide for the equitable treatment of its members, to defray reasonable expenses of its members:

association are designed to prevent unjust acts and practices, to promote just and equitable principles of trade, to provide safeguards against unreasonable rates of commissions or discounts, to protect investors and the public interest, to protect investors and the public interest, to prevent impediments to and perfect the mechanism of the market; and are not designed to permit unfair competition between customers or issuers, or brokers or dealers, or to impose any schedule of

prices, or to impose any schedule or fix minimum rates of commissions, allowances, discounts, or other charges;

"(8) the rules of the association provide that its 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 any 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 satisfied. 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 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 operate as a stay of such action until an order is issued upon such review pursuant to subsection (h).

"(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 deter-

ions provided by the rules of said association in accordance with subsection

of its rules satisfy the requirements (5) to (9), inclusive, of subsection (a) of any such association any rule therein of the type authorized in subsection (b) shall not be less stringent than the rules of a national securities association with which it is affiliated.

Upon application for registration pursuant to subsection (d), the Commission shall by order determine whether the requirements of this section are satisfied. After notice and opportunity for hearing, the Commission shall by order deny such registration if the applicant is not a registered national securities association or if the applicant shall fail to be admitted to membership with a registered national securities association. The Commission shall revoke the registration of such

an association (whether national or otherwise) if, after reasonable notice as the Commission may determine for the protection of investors, it is found by filing with the Commission a written statement in such form as the Commission may prescribe. Upon the withdrawal of a statement or the expiration of a period from registration, the registration of such association shall automatically terminate. Any disciplinary action (whether national or otherwise) against any member of such association or any broker or dealer seeking membership therein shall be subject to review by the Commission upon application by any person within sixty days after such action has been taken, if as the Commission may determine, such review, or the institution of review thereon, shall operate as a stay of the action issued upon such review pursuant to

such review disciplinary action taken by a national securities association against a member thereof, if the Commission, after notice and opportunity for hearing, and before the association and such other persons as may be relevant, shall (A) find that such acts or practices, or has omitted such acts or practices, or has omitted such acts or practices, or omission of such acts or practices, or omission of such acts or practices, as have been found to be in violation of the rules of the association, the Commission shall, unless it appears to the Commission that the action should be modified in accordance with paragraph (b), by order deny such registration. The Commission shall likewise deter-

mine 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 designated rule or rules, the Commission shall by order set aside the action 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, 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 nonmember 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 'nonmember 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). Any change in or addition to the rules of a registered securities association shall take effect upon the thirtieth day after the filing of a copy thereof with the Commission, or upon such earlier date as the Commission may determine, unless the Commission

shall enter an order disapproving such change or addition; and the Commission shall enter such an order unless such change or addition appears to the Commission to be consistent with the requirements of subsection (b) and subsection (d).

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

"(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; and (4) affiliation between registered securities associations.

"(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 or 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 any rule or regulation thereunder, or has failed to enforce compliance with its own rules, or has engaged in any other activity tending to defeat 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 (A) has violated any provision of this title or any rule or regulation thereunder, or has effected any transaction for any other person who, he had reason to believe, was violating with respect to such transaction any provision of this title or any rule or regulation thereunder, or (B) has willfully violated any provision of the Securities Act of 1933, as amended, or of any rule or regulation thereunder, or has effected any transaction for any other person who, he had reason to believe, was willfully violating with respect to such transaction any provision of such Act or rule or regulation;

"(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 willfully failed to enforce the rules of the association, or has willfully abused his authority.

such change or addition; and the order unless such change or addition is consistent with the requirements of (2).

is authorized by order to abrogate any association, if after appropriate notice it appears to the Commission that such is appropriate to assure fair dealing by the to assure a fair representation of its of its affairs or otherwise to protect uses of this title.

in writing request any registered secur- specified alteration of or supplement to of the matters hereinafter enumerated. to such alteration or supplement within tion is authorized by order to alter association in the manner theretofore notice and opportunity for hearing, it such alteration or supplement is neces- sary in the public interest or for the protection of purposes of this section, with respect to: (1) the method for the election of members; (2) the method for adop- ing to the rules of the association; (3) the election of directors; and (4) affiliation between

is authorized, if such action appears to it to be in the public interest or for the protection of purposes of this section—

notice and opportunity for hearing, a period not exceeding twelve months of a registered securities association, that such association has violated any rule or regulation thereunder, or has acted in violation of its own rules, or has engaged in any act or practice which tends to defeat the purposes of this section; notice and opportunity for hearing, by a period not exceeding twelve months or to securities association any member thereof is (A) has violated any provision of this section thereunder, or has effected any act or practice in violation of any provision of this section, or (B) has willfully violated any provision of the Securities Act of 1933, as amended, or any rule or regulation thereunder, or has effected any act or practice in violation of any other provision of the Securities Act of 1933, as amended, or any rule or regulation thereunder, or has engaged in any act or practice in violation of any rule or regulation; notice and opportunity for hearing, by a period not exceeding twelve months or to securities association any member thereof is (A) has violated any provision of this section thereunder, or has effected any act or practice in violation of any provision of this section, or (B) has willfully violated any provision of the Securities Act of 1933, as amended, or any rule or regulation thereunder, or has effected any act or practice in violation of any other provision of the Securities Act of 1933, as amended, or any rule or regulation thereunder, or has engaged in any act or practice in violation of any rule or regulation;

notice and opportunity for hearing, by a period not exceeding twelve months or to securities association any member thereof is (A) has violated any provision of this section thereunder, or has effected any act or practice in violation of any provision of this section, or (B) has willfully violated any provision of the Securities Act of 1933, as amended, or any rule or regulation thereunder, or has effected any act or practice in violation of any other provision of the Securities Act of 1933, as amended, or any rule or regulation thereunder, or has engaged in any act or practice in violation of any rule or regulation;

"(m) Nothing in this section shall be construed to apply with respect to any transaction by a broker or dealer in any exempted security.

"(n) 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."

SEC. 2. Subsection (c) of section 15 of such Act, as amended, is amended to read as follows:

"(c) (1) No broker or dealer shall make 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 (other than commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, by means of any manipulative, deceptive, or other fraudulent device or contrivance. The Commission shall, for the purposes of this subsection, by rules and regulations define such devices or contrivances as are manipulative, deceptive, or otherwise fraudulent.

"(2) No broker or dealer shall make use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, in connection with which such broker or dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation. The Commission shall, for the purposes of this paragraph, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative and such quotations as are fictitious.

"(3) No broker or dealer shall make use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors to provide safeguards with respect to the financial responsibility of brokers and dealers."

SEC. 3. Subsection (b) of section 20 of such Act is amended by inserting before the period at the end thereof a colon and the following: "Provided, (A) That no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 15 of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 15 of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation".

SEC. 4. Section 32 of such Act, as amended, is amended by adding at the end thereof the following new subsection:

"(c) The provisions of this section shall not apply in the case of any violation of any rule or regulation prescribed pursuant to paragraph (3) of subsection (c) of section 15 of this title, except a violation which consists of making, or causing to be made, any statement in any report or document required to be filed under any such rule or regulation, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact."

SEC. 5. Subsection (a) of section 17 of such Act, as amended, is amended by inserting immediately after the words "every broker or dealer who transacts a business in securities through the medium of any such member," the words "every registered securities association,".

Approved, June 25, 1938.

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