



DIVISION OF
MARKET REGULATION

Lee
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

RECEIVED

MAY 24 1973

E. S. COMM.

MAY 23 1973

Office of

MAY 24 1973

Senator John Sparkman

Honorable John Sparkman
Chairman
Committee on Banking, Housing
and Urban Affairs
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

The Commission has asked me to forward to you for your information a copy (enclosed) of our letter transmitting to the President and the Congress, pursuant to Section 7(c)(2) of the Securities Investor Protection Act, the Second Annual Report of the Securities Investor Protection Corporation.

Sincerely yours,

Lee A. Pickard
Director

Enclosure

C O P Y

The President of the United States
The President of the Senate
The Speaker of the House of Representatives

Gentlemen:

I have the honor on behalf of the Securities and Exchange Commission to transmit herewith, pursuant to Section 7(c)(2) of the Securities Investor Protection Act of 1970 ("the Act"), the Second Annual Report of the Securities Investor Protection Corporation ("the Corporation"), covering the year 1972. Section 7(c)(2) of the Act requires the Corporation to submit its Annual Report to the Commission, and also requires the Commission to transmit such Report to the President and the Congress "with such comment thereon as the Commission may deem appropriate." Our comments follow:

As its Report reveals, the Corporation is discharging its difficult functions with efficiency and economy. This is no small accomplishment, since the Corporation represents a unique concept ^{1/} and was born during a troubled period in the history of the securities industry. Credit is due to the wisdom of Congress in framing this legislation and to the very able leadership and management which the Corporation has been fortunate enough to receive.

The Corporation's Report refers to a number of problems which it has encountered. As noted on page 25 and in the Appendices to the Corporation's Report, a substantial number of broker-dealers which have had to be liquidated by the

1/ The Corporation differs from the Federal Deposit Insurance Corporation, which was referred to as a model during the Congressional debates on the Act, in a number of significant ways. Among these are the fact that the FDIC is, to an important degree, a regulatory agency, while the Corporation is not, as a result of a decision of the Congress, supported by the Commission, not to interject another level of regulation into the self-regulatory pattern of the securities industry. Further, the Corporation is not entitled to select the risks which it will insure.

Corporation, failed by reason of illegal conduct, including failure to maintain the required books and records or fraudulent or manipulative activities. Inadequate capital was also a factor, and it is significant that appreciably more than half the firms in liquidation had been in business for only three years or less. As described in the Commission's Annual Report for the Fiscal Year ended June 30, 1972, particularly at pages 57-60, and in Chairman Casey's introduction, the Commission and the self-regulatory bodies have taken various steps to strengthen the capital and other requirements for new firms and to improve the broker-dealer examination programs, both of the Commission and the self-regulatory bodies, with particular emphasis upon the early examination of new firms and the development of early warning systems for the detection of financial and operational problems of broker-dealers. It is hoped that these measures will reduce the number of cases in which the Corporation is required to undertake liquidation. Fortunately, at least so far, the Corporation has not been required to undertake liquidation of any really large firm.

The liquidation procedures employed by the Corporation are modeled, in large part, upon those contained in the existing bankruptcy laws. In many of these liquidations, the Corporation has encountered problems which perhaps were not fully anticipated when the Act was under consideration. These include the delay and expense resulting from inadequate records of the broker-dealers and the problems of detecting and investigating fraudulent claims against the Corporation, which may have been manufactured by the principals of firms approaching failure or their accomplices.

The Corporation has also encountered some difficulty in the prompt and complete collection of the assessments due it. In significant part, this resulted from the number of firms which had simply gone out of business as a result of current conditions in the securities industry. It is hoped that the revised procedures, referred to on pages 13 and 14 of the Corporation's Report, will alleviate this problem.

Page Three

Some of the foregoing matters, as well as other questions discussed in the Corporation's Report, might point to the desirability of considering possible amendments to the Act. We believe, however, the Act has, in the main, worked well and that in view of the limited experience with its administration, consideration of amendments at this time would probably be premature.

Respectfully submitted,

Hugh F. Owens
Senior Commissioner