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75TH CONDERSE) HOUSE OF REPRESENTATIVES.

REPORT No. 2307

REGULATION OF OVER-THE-COUNTER MARKETS

May 6, 1938.-Committed to the Committee of the Whole House on the state of the Union and ordered to be printed

Mr. EICHER, from the Committee on Interstate and Foreign Commerce, submitted the following

REPORT

[To accompany S. 3255]

The Committee on Interstate and Foreign Commerce, to whom was referred the bill (S. 3255) 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, having considered the same, report favorably thereon with unendments and recommend that the bill as amended do pass.

The amendments recommended by the committee are as follows:

In subsection (f) of the amendment made by section 1 of the bill strike out ", but such withdrawal shall be subject to such appropriate terms and conditions for the orderly liquidation of such association as the Commission may prescribe".

Amend section 2 of the bill to read as follows:

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 tother than commercial paper, bankers acceptances, or commercial fulls) otherwise than on a national scourities exchange, by means of any maniputative, deceptive, or other fraudulent device or contriv-The Commission shall, for the purposes of this subsection, by rules and ance. 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 inatramentality of interstate commerce to effort any transaction in, or to induce or attempt to induce the parchase or sale of, any scenarity (other than an exempted security or commercial paper, bankers' torreptances, or commercial bills) otherwise than on a national scenarios exchange, in connection, with which such broker or dealer engages in any fraudulent, deceptive, or munipulative act or practice, or makes may fictitions quotation. The Commission shull, for the purposes of this makes noy fightitions quotation. paragraph, by rules and regulations define, and prescribe means reasonably de-

signed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative and such quotations as are fictitions.

"(3) No broker or dealer shall make use of the mails or of any means of instrumentality al interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any seconity (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national scentities 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 (A) to provide safeguards with respect to the financial responsibility of brokers and dealers; (B) to regulate the manner, method, and place of soliciting business; and (C) to regulate the time and method of making settlements, payments, or deliveries."

Amend section 3 of the bill to read as follows:

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 (3) of subsection (c) of Section 15 of this title, and (l) 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 deater sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation pr.sectibed pursuant to paragraph (1) or (2) of subsection (c) of section 15 of this subsection is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation."

In the amendment made by section 4 of the bill strike out "pursuant to clause (3), (4), or (5) of subsection (c)" and insert in lieu thereof "pursuant to paragraph (3) of subsection (c)".

I

GENERAL STATEMENT

A. INTRODUCTORY

Sonate bill 3255 amends the Securities Exchange Act of 1934, as amended, by inserting a new section, section 15A, immediately after the present section 15; and by amending subsection (c) of section 15, subsection (b) of section 29, section 32, and subsection (a) of section 17. In its essentials, the new section 15A would set up a system for cooperative regulation of the over-the-counter markets, through the activities of voluntary associations of investment bankers, dealers, and brokers doing business in these markets, under appropriate goveramental supervision. The proposed amendment of subsection (c) of section 15 of the Securities Exchange Act would clarify and strengthen the direct regulatory powers over the over-the-counter markets embodied in the present subsection (c), and would provide for certain additional direct powers which are desirable in the public interest. The changes in sections 29, 32, and 17 are supplementary to the new section 15A and the changes in subsection (c) of section 15.

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D. SCOPE OF THE PROBLEM

1. Importance of the over-the-counter markets.---Under the Securities Exchange Act of 1934, the over-the-counter markets are deemed to include all transactions in securities which take place otherwise than upon a national securities exchange. These markets are immense, the activities embraced therein are varied, and they are of the utmost importance to the national economy.

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read as follows:

of such Act is amended by inserting before and the following: "Provided, (A) That no is Expection because of any violation of any is paragraph (3) of subsection (c) of Sectract shall be deemed to be void by reason inted in reliance upon this subsection, by r or dealer sells, or from or for whom any in violation of any rule or regulation pr.-1 of subsection (c) of section 15 of this Lin one year after the discovery that such and within three years after such violation."

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ecurities Exchange Act of 1934, as ion, section 15A, immediately after Ending subsection (c) of section 15, or 32, and subsection (a) of section tion 15A would set up a system for s-the-counter markets, through the is of investment bankers, dealers, se markets, under appropriate govused amendment of subsection (c) of pe Act would clarify and strengthen the over-the-counter markets emc), and would provide for certain be desirable in the public interest.

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REGULATION OF OVER-THE-COUNTER MARKETS 3

Currently, some 6,766 firms of brokers and dealers are registered with the Commission is transacting business in the over-the-counter markets. For purposes of comparison, it may be pointed out that there are only 1,375 members of the New York Stock Exchange. Over-the-counter quotations for at least 60,000 separate issues of securities are published in services to which brokers and dealers subscribe, whereas only about 6,000 separate issues of stocks and bonds are admitted to trading on all the stock exchanges of the country,

Moreover, a great deal of trading takes place over the counter even in securities which are admitted to trading upon exchanges. This is particularly true of high-grade bonds and preferred stocks; in fact, many issues of high-grade bonds and preferred stocks are not admitted to trading upon any exchange, and have their only market over the counter. For example, an estimate indicates that, as of the summer of 1937, insurance company securities with an approximate market value of about \$343,000,000 were admitted to trading upon exchanges. whereas some \$1,209,000,000 of insurance company securities-roughly four times the previous figure-were not admitted to trading upon any exchange, and thus enjoyed their only market over the counter. Moreover, the primary operations of the great underwriting houses take place over the counter. Thus, the over-the-counter markets not only provide the medium for an immense volume of trading in a great variety of securities, but they also provide the principal channel by which the savings of the Nation flow into new financing. It is scarcely necessary to state the importance of the process by which the financial requirements of expanding industry are nict through the public sale of securities to investors. The process of distributing such securities takes place on a national scale over the counter.

The over-the-counter markets in their day-to-day operation may be envisaged as a network of telephone and telegraph wires connecting dealers in all parts of the country. One might almost describe the interstate telephone as a trade symbol for this highly important business. The mails, of course, are used extensively and continuously. Thus, the over-the-counter markets are national in a dual sense: First, because of their immense importance to the national economy; second, because the actual operations of these markets are interconnected on a national scale.

2. Importance of regulating the over-the-counter markets in relation to the regulation of exchanges.—The importance of the over-the-counter markets in and of themselves would suffice to justify a reasonable system of regulation. Effective regulation of these markets is, moreover, imperative to prevent the evasion of the system of regulation of exchange trading embodied in the Securities Exchange Act of 1934. This was recognized by the Congress in the original enactment of that act. Thus, the report of the Senate Committee on Banking and Currency (S. Rept. No. 792, 73d Cong., 2d sess.) accompanying the bill which became the Securities Exchange Act of 1934 included the following statements:

It has been deemed advisable to authorize the Commission to subject such activities [i. c., trading in the over-the-counter markets] to regulation similar to that prescribed for transactions on organized exchanges. This power is vitally necessary to forestall the widespread evision of stock-exchange regulation by the withdrawal of securities from listing on exchanges, and by transferring trading therein to "fover-the-counter" markets where manipulative evils could continue to flourish, unchecked by any regulatory authority (p. 6).

Similarly, the report of the House Committee on Interstate and Foreign Commerce (H. Rept. No. 1383, 73d Cong., 2d sess.) accompanying the House bill for the regulation of exchanges quotes with approval the following statement from the report of the Twentieth Century Fund on Stock Market Control:

To leave the over-the-counter markets out of a regulatory system would be to destroy the effects of regulating the organized exchanges (p. 16).

These statements remain no less true today.

3. Abuses in the over-the-connter markets.-A single phase of the administrative experience of the Securities and Exchange Commission suffices to illustrate the extent of the problem of policing the submarginal element among over-the-counter brokers and dealers. In 1937, the Commission made investigations in three areas outside the largest financial centers-in Cleveland, Detroit, and the Pacific Northwest. A few attorneys and accountants were sent to these areas to inquire into certain complaints and to make a brief survey. In the space of a few months 13 individuals were criminally convicted, 16 more were placed under indictment, 17 corporations and 41 more individuals were enjoined, and 2 firms were expelled or obliged to withdraw from national securities exchanges, all for elementary violations of the law. These results produced by so limited a staff within three restricted areas in so short a time speak for themselves. We are advised that the Commission has every reason to believe that the problem revealed thereby exists in other regions as well.

4. Nature of the problem of regulation.—The problem of regulation of the over-the-counter markets has three aspects: First, to protect the investor and the honest dealer alike from dishonest and unfair practices by the submarginal element in the industry; second, to cope with those methods of doing business which, while technically outside the area of definite illegality, are nevertheless unfair both to customer and to decent competitor, and are seriously damaging to the mechanism of the free and open market; and, third, to afford to the investor an economic service the efficiency of which will be commensurate with its economic importance, so that the machinery of the Nation's markets will operate to avoid the misdirection of the Nation's savings, which contributes powerfully toward economic depressions and breeds distrust of our financial processes.

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The committee believes that there are two alternative programs by which this problem could be met. The first would involve a pronounced expansion of the organization of the Securities and Exchange Commission; the multiplication of branch offices; a large increase in the expenditure of public funds; an increase in the problem of avoiding the evils of bureaucracy; and a minute, detailed, and rigid regulation of business conduct by law. It might very well mean expanding the present process of registration of brokers and dealers with the Courmission to include the proscription not only of the dishonest, but also of those unwilling or mubble to conform to rigid standards of financial responsibility, professional conduct, and technical proficiency. The second of these alternative programs, which the committee believes distinctly preferable to the first, is embodied in S. 3255, "This-program is based upon cooperative regulation, in which the task will be largely performed by representative organizations of investment bankers, dealers, and brokers, with the Government exercising appropriate supervision in the public interest, and exercising supplementary

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powers of direct regulation \geq In the concept of a really well organized and well-conducted stock exchange, under the supervision provided by the Secruities Exchange Act of 1934, one may perceive something of the possibilities of such a program.

C. LEGISLATIVE UACKGROUND

In the Securities Exchange Act of 1934, as originally enacted, the over-the-counter markets were dealt with, in brief outline, in a single The brevity and generality of this treatment arose from a section. realistic recognition of the great difficulties of working out in any detail a suitable plan of regulation at that time, in view of the fact that so little was then known concerning these markets. But, though the Congress did not at that time have before it a sufficient record of data or experience to enable it to determine upon a detailed plan of regulation, it clearly set forth the objectives of and the standards for such regulation. Section 15, in its original form, expressly contemplated the adoption by the Securities and Exchange Commission of rules and regulations concerning the over-the-counter markets "necessary or appropriate in the public interest to insure to investors protection comparable to that provided by and under authority of this title in the case of antional securities exchanges". To that end, the Commission was authorized to adopt rules and regulations providing "for the regulation of all transactions by brokers and dealers on any such market, for the registration with the Commission of dealers and/or brokers making or creating such a market, and for the registration of the securities for which they make or create a market."

After a year and a half of administrative experience under the original section 15, that section was, in May 1936, amended to embody the results of that experience. In consequence, section 15 in its present form is far more specific than in its original form. Since that amendment, another year and a half of administrative experience has been accumulated. This experience has both demonstrated the need and laid the foundation for a further step, which is taken in the bill now under consideration. In the judgment of the committee this bill, like the amendment of section 15 enacted in May 1930, does not enlarge the objectives or the outline of regulatory functions initially set forth in the original section 15. On the contrary, it represents the essential process of filling in and implementing the original outline in order to make possible the realization of the original objectives.

D. DROWTH OF THE IDEA OF COOPERATIVE REGULATION

The plan of cooperative regulation embodied in S. 3255 rests upon 3 years of gradual and orderly growth. Almost from its inception, the Commission conducted extended conferences with representatives of various associations of investment bankers, dealers, and brokers from all parts of the country. About 3 years ago a conference committee was formed, representative of the industry, to obtain the views of investment bankers, dealers, and brokers as to the desirability of perfecting a permanent scheme of organization for the purposes hereinabove discussed. As a result of the activities of the conference committee, there came into existence in 1936 an organization known as the Investment Bankers Conference, Inc. This organization has

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enrolled and maintained a membership, the committee is informed, of some 1,700 firms situated in all parts of the United States. There are likewise in existence in the country a number of other associations of brokers and dealers which have for some time exercised a degree of supervision over the conduct of their members.

The committee believes that these years of experiment in organization among members of the industry and in the development of their relations with the Commission provide a sound and practical basis for the program embodied in S. 3255.

II

ANALYSIS OF THE BILL BY SECTIONS.

A. SECTION 1

Section 1 would amend the Securities Exchange Act of 1934, as amended, by inserting after section 15 thereof a new section, section 15A.

1. Subsection (a) of section 15A.—This subsection provides that essociations of brokers or dealers may register with the Commission as national securities associations pursuant to subsection (b), or as affiliated securities associations pursuant to subsection (d), under stated terms and conditions, upon the filing of certain specified data. This subsection is similar to subsection (a) of section 6 of the Securities Exchange Act of 1934, as amended, which provides for the registration of national securities exchanges, except that associations which do not register are not denied the use of the mails or instrumentalities of interstate commerce. Thus, the formation of associations and application for registration by them are matters of voluntary choice. It should be noted that membership by a broker or dealer in such a registered securities association does not supersede the obligation of individual brokers or dealers to register under section 15 of the Exchange Act.

2. Subsection (b) of section 15A.—This subsection sets forth requirements which an association of brokers or dealers must satisfy to qualify for the registration as a national securities association. The requirements are enumerated in 10 paragraphs, a discussion of which follows:

(a) Paragraph (1) of subsection (b): This paragraph limits eligibility for registration as a national securities association to such associations as are a proper subject of national concern. It is contemplated that associations, to qualify under this paragraph, should either be actually Nation-wide in scope or should represent a substantial and economically cohesive region. Without suggesting that such regions should necessarily be identical with the districts under the Federal Reserve System, such districts may perhaps be cited as an illustration of the type of tegion which would be appropriate.

(b) Paragraph (2) of subsection (b): This paragraph limits elicibility for registration as a national scentrities association to associations of which this general pattern of organization and general character ar such as to satisfy the Commission that they will be able effectually to discharge their function of carrying out the purposes of the new section 15A within the framework of the Exchange Act.

(c) Paragraph (3) of subsection (b): The broad purpose of this paragraph is to make sure that all brokers and dealers who conduct

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15A.—This subsection provides that silers may register with the Commission stions pursuant to subsection (b), or as ics pursuant to subsection (d), under pounts to filing of certain specified data. Section (a) of section 6 of the Securities inded, which provides for the registration except that associations which do not be of the mails or instrumentalities of the formation of associations and appliing are matters of voluntary choice. It is does not supersede the obligation of the register under section 15 of the

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an honest and responsible business shall be eligible for membership in some association. Particular associations may, however, by their rules restrict membership therein on such specified geographical basis, such specified basis relating to the type of business done by their 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 public interest or for the protection of investors and to carry out the public interest initial to brokers and dealers from some designated geographical region, or to brokers and dealers transacting business exclusively in a particular class of securities, may be eligible for registration. Any geographical restrictions upon membership, however, must be broad enough to satisfy the requirements of paragraph (1).

(d) Paragraph (4) of subsection (b): The broad purpose of this paragraph is to exclude from membership in any registered securities association any broker or dealer who has disqualified himself by improper conduct. Thus, a broker or dealer may not be admitted to or continued in membership in a registered securities association (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) if he has been and is expelled or suspended from another registered securities association for a serious infraction of its rules; or if he has been and is expelled or subunded from a national securities exchange for a serious infraction of its rides; or if an order of the Commission is in effect denying or revoking his registration pursuant to section 15 of the Exchange Act; or if an order of the Commission is in effect expelling or suspending him from membership in a registered securities association or a national securities exchange; or, finally, if his conduct while employed by, acting for, or directly or indirectly controlling or controlled by a braker or dealer, was a cause which contributed to any suspension, expulsion, or order of the character described above which is in effect with respect to such broker or dealer. To prevent the evasion of these requirements, this paragraph also provides that a broker or dealer shall be incligible for membership in a registered securities association if any person who is currently a partner, officer, director, or branch manager of such broker or dealer (or who currently occupies a similar status or performs similar functions) or who currently controls or is controlled by such broker or dealer, is subject to any suspension, expulsion, or order of the kind described above, or was a cause of any such suspension, expulsion, or order which is currently in effect.

(c) Paragraph (5) of subsection (b): This paragraph is designed to assure to each member of a registered securities association reasonable representation in all phases of its operations.

(f) Paragraph (6) of subsection (b): This paragraph has a dual purpose: First, to provide that the total of dues assessed against the members of an association shall not exceed an amount necessary to defray reasonable expenses of administration; second, to provide that such dues shall be fairly allocated among the members of the association.

(g) Paragraph (7) of subsection (b): This paragraph outlines the functions for the accomplishment of which registered securities associations are expected to accept responsibility. To be eligible for registration, the rules of an association must be designed to prevent frandulent and manipulative acts and practices, to provide safeguards

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against unreasonable profits or unreasonable rates of commissions or other charges, to promote just and equitable principles of trade, 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. As safeguards against abuse, and to make clear that activities of associations under this paragraph are to be consistent with the operation of free and open markets, this paragraph provides that the rules of an association may not be designed to permit unfair discrimination. between customers, or issuers, or brokers or dealers, nor to fix minimum profits, nor to impose any schedule of prices, nor to fix minimum rates or impose any schedule of commissions, allowances, discounts, or other charges. Thus, to provide safeguards against unreasonable profits, it is contemplated that associations may adopt rules designed to prevent each member Gercof from exacting in any particular transaction a profit which reasonable men would agree was unconscionable in the light of all of the concrete facts and circumstances of that transaction; but an association, whether in a bona fide attempt to prevent or under the protext of preventing unreasonable profits, may not impose any schedule of prices or commissions.

(\hbar) Paragraph (8) of subsection (b): This paragraph limits eligibility for registration to associations, the rules of which provide that members shall be appropriately disciplined for violations of its rules. Disciplining may be in the form of expulsion, suspension, line, censure, or any other fitting penalty. The form of discipline in any case must be appropriate to the particular violation.

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(i) Parngraph (9) of subsection (b): This paragraph outlines the essential elements of a fair and orderly procedure to which associations must adhere in proceedings to discipline members or to deny membership to applicants. It is contemplated that the exact procedure will be defined by the rules of the association, within the framework set forth in this paragraph.

(j) Paragraph (10) of subsection (b): This paragraph provides simply that the requirements of subsection (c), to the extent that these may be applicable, must be satisfied.

3. Subsection (c) of section 15A.—Under this subsection, an association registered as a national securities association pursuant to subsection (b) may be required or permitted to provide for the admission of an association registered as an uffiliated securities association pursuant to subsection (d) to participation in such national securities association as an affiliate, upon certain terms and conditions. The purpose of this paragraph is to enable soundly organized associations of brokers and dealers which are local in character, and hence not eligible for registration as national securities associations pursuant to subsection (b), to retain their identity as registered associations, if, by affiliation with a national securities association, they bring themselves within a sphere which is a proper subject of national concern and make possible coordinated administration.

4. Subsection (d) of section 15.1.—This subsection sets forth requirements which must be satisfied by a local association which is seeking registration as an affiliated securities association. In general, these requirements are parallel to those set forth in subsection (h): but there are in addition certain requirements which are applicable only to this kind of association.

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or unreasonable rates of commissions or and equitable principles of trade, and, s and the public interest, and to remove ie mechanism of a free and open market. . and to make clear that activities of aph are to be consistent with the operai, this paragraph provides that the rules designed to permit unfair discrimination or brokers or dealers, nor to fix minimum scile of prices, nor to fix minimum rates missions, allowances, discounts, or other erguards against unreasonable profits, tions may adopt rules designed to prec exacting in any particular transaction sould agree was unconscionable in the and circumstances of that transaction; s long fide attempt to prevent or under seconable profits, may not impose any 12.

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5. Subsection (e) of section 15A.—This subsection relates to the mechanics of granting or denying registration of associations pursuant to subsection (b) and subsection (d).

6. Subsection (f) of section 15A.—Under this subsection, amended as proposed, a registered securities association may, upon such reasonable notice as the Commission may prescribe as necessary in the public interest or for the protection of investors, withdraw from registration by liting a written notice of withdrawal in due form.

7. Subsection (g) of section 15A.—This subsection provides that any disciplinary action taken by a registered securities association against any member, and any action taken by such association denying admission to an applicant for membership, shall be subject to review by the Commission. Application to the Commission for review, or the institution of review by the Commission on its own motion, automatically stays the action of the association pending review by the Commission pursuant to subsection (h). 8. Subsection (h) of section 15A.—This subsection sets forth the

8. Subsection (h) of section 15.1.—This subsection sets forth the essential elements of the procedure to be followed by the Commission in reviewing any disciplinary action or any action denying membership which has been taken by a registered securities accountion.

which has been taken by a registered securities areodution. 9. Subsection (i) of section 13A.—Broadly stated, under this subsection, a registered securities association may by its rules provide that no member thereof shall do business with any broker or dealer who is not a member of any registered securities association, except at the same prices, for the same commissions or fees, and on the same terms and conditions as are accorded to the general public by such member. Thus, it is contemplated that exclusion from membership in a registered securities association will be attended and implemented by economic sanctions. In this respect, exclusion from such an association would be comparable in effect to expulsion from a national securities exchange. It is these economic sanctions which would make possible effective discipline within the association.

It should be noted that nothing in this paragraph purports to authorize an association by its rules to prescribe any uniform differences between prices charged or discounts allowed to brokers and dealers, on the one hand, and members of the public, on the other hand, to which members of the association must adhere. Any such rule would be in derogation of paragraph (7) of subsection (b). The individual member is left free to determine his own business policy, but, insofar as he differentiates in prices, discounts, and other charges or allowances between brokers and dealers and members of the public, the rules of the association may require him to classify "nonmember brokers or dealers" with members of the public.

brokers or dealers" with members of the public. 10. Subsection (j) of section 15A.—This subsection requires registered securities associations to file with the Commission in accordance with such rules and regulations as the Commission may prescribe any information or documents necessary to keep current or to supplement the original registration statement and documents filed therewith, as well as copies of any changes in or additions to the rules of the association. No change in or addition to the rules of a registered securities association shall take effect until the thirtieth day after filing or until such earlier date as the Commission may determine; and the Commission is empowered and directed by order to prevent such change or addition from taking effect, unless such change or 10. Nept. 2307, 75-3--2

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addition appears to the Commission to be consistent with the requirements of subsection (b) and subsection (d).

11. Subsection (k) of section 15.1.—Under this subsection, the Commission is authorized by order to abrogate any rule of a registered securities association, after appropriate notice and opportunity for hearing, if this appears to the Commission to be necessary or appropriate to assure fair dealing by the members of the association, to assure a fair representation of its members of the association of its affairs, or otherwise to protect investors or effectuate the purposes of this title. The Commission may, moreover, by order alter or supplement the rules of an association with respect to four enumerated subjects, each of which relates to the organization and operation of the association as such, and not to the business conduct of the individual members; but the Commission may thus alter or supplement the rules of an association only if it has first in writing requested the association to adopt the specified alteration or supplement, and only after appropriate notice and opportunity for hearing.

12. Subsection (1) of section 15A.—Under this subsection the Commission is authorized in appropriate cases, upon specified terms and conditions, and after appropriate notice and opportunity for hearing, by order to suspend or revoke the registration of a registered securities association, to suspend or expel members from a registered securities association, or to remove any officer or director of a registered securities association. These supervisory powers are designed to prevent abuse, and to enable the Commission effectually to discharge its role in this scheme of cooperative regulation.

13. Subsection (m) of section 15A.—This subsection provides that section 15A shall not be construed to apply with respect to transactions by brokers or dealers in exempted securities. "Exempted securities" are defined by section 3 (a) (12) of the Exchange Act to include various forms of Government, State, municipal, and other public securities.

14. Subsection (n) of section 15A.--This subsection provides that if any provision of section 15A should be in conflict with any provision of any law of the United States in force on the date when the bill under consideration takes effect, the provision of section 15A shall prevail.

B. SECTION 2

Section 2, amended as proposed by the committee, amends subsection (c) of section 15 of the Securities Exchange Act of 1934, as amended. In effect, two new paragraphs are added to the present subsection (c); the present subsection (c) becomes paragraph (1) of the proposed new subsection (c), and the two new paragraphs are numbered (2) and (3), respectively. Subsection (c) relates to the direct powers of the Commission to adopt rules generally applicable to over-the-counter brokers and dealers.

As has been explained, paragraph (1) of the proposed new subsection (c) is identical with the present subsection (c), under which the Commission has adopted rules and regulations which have withstood the test of experience and have met with the approval of representative groups of brokers and dealers subject thereto. It is contemplated that rules of similar character and additional appropriate rules will be adopted under paragraph (1) of the proposed new subsection (c).

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distion to be consistent with the requireresection (d).

5.1.—Under this subsection, the Comev to abrogate any rule of a registered appropriate notice and opportunity for e Commission to be necessary or approip the members of the association, to with members in the administration of text investors or effect inter the purposes ion may, moreover, by order after or whisting many moreover, by order after or whisting with respect to four enumerated to the organization and operation of the othe business conduct of the individual ion may thus after or supplement the if it has first in writing requested the ifed alteration or supplement, and only opportunity for hearing.

3.4.—Under this subsection the Comstriate cases, upon specified terms and inte notice and opportunity for hearing, the registration of a registered securities is members from a registered securities y officer or director of a registered semervisory powers are designed to pre-Commission effectually to discharge its the regulation.

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SECTION 2

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Paragraph (2) of the proposed new subsection (c), which does not apply to transactions in exempted securities, clarifies and broadcas the power of the Commission by rules and regulations to prevent fraudulent, manipulative, and deceptive acts and practices and fictitious quotations.

Paragraph (3) of the proposed new subsection (c), which likewise does not apply to transactious in exempted securities, empowers the Commission by rule and regulation to take action against certain other abuses and to promote orderly and efficient business practices in connection with specified subjects.

The need of these additional powers has been demonstrated by the administrative experience of the Commission. Thus, paragraphs (2) and (3) represent a necessary step forward toward realizing the original objectives and implementing the original standards of regulation set forth in section 15 of the Exchange Act in its original form.

C. SECTION 3

Section 3, amended as proposed by the committee, amends subsection (b) of section 29 of the Exchange Act to provide that contracts entered into in violation of any rule or regulation under paragraph (3) of the proposed new subsection (c) shall not be void by reason of subsection (b) of section 29, and that no contract is to be deemed void by reason of this subsection in an action maintained in reliance upon the subsection involving a violation of any rule or regulation prescribed pursuant to paragraph (1) or (2) of section 15 (c), unless such action is brought within 1 year after discovery that the sale or purchase involves such violation and within 3 years after such violation.

D. SECTION 4

The committee recommends that section 4 be amended by striking the words "pursuant to clause 3, 4, or 5 of subsection (c)" and substituting the words "pursuant to paragraph (3) of subsection (c)." This change follows us a matter of course from the change in the proposed new subsection (c), which has been discussed above: paragraph (3) of subsection (c), as amended in accordance with the recommendation of the committee, corresponds in substance to clauses 3, 4, and 5 of the proposed new subsection (c) embodied in section 2 of the bill as passed by the Senate.

E. SECTION 5

This section amends subsection (a) of section 17 of the Exchange Act to subject every registered securities association to the same duties in regard to the keeping of records and the making of reports as, under the terms of that subsection, now devolve upon every registered broker or dealer, every national securities exchange, every member of any national securities exchange, and every broker or dealer who transnets a business in securities through the medium of any such member.

CHANGES IN EXISTING LAW

In compliance with paragraph 2a of rule XIII of the Rules of the House of Representatives, changes in the Scentities Exchange Act of 1934 made by the bill are shown as follows: Existing law proposed

to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in rouman.

SEC. 15. (s) No broker or dealer (other than one whose business is exclusively intrastate) 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 scenarity (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a mational securities exchange, unless such broker or dealer is registered in accordance with subsection (b) of this section.

(b) A broker or dealer may be registered for the purposes of this section by filling with the Commission an application for registration, which shall contain such information in such detail as to such broker or dealer and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such broker or dealer, as the Commission may by rules and regulations require as necessary or appropriate in the public interest or for the protection of investors. Except as hereinafter provided, such registration shall become effective thirty days after the receipt of such application by the Commission or within such shorter period of time as the Commission may determine.

An application for registration of a broker or dealer to be formed or organized may be made by a broker or dealer to which the broker or dealer to be formed or organized is to be the successor. Such application shall contain such biformation in such detail as to the applicant and as to the successor and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, the applicant or the successor, as the Commission may by rules and regulations require as uccessary or appropriate in the public interest or for the protection of investors. Except as hereinafter provided, such registration shall become effective thirty days after the receipt of such application by the Commission or within such shorter period of time as the Commission may determine. Such registration shall terminate on the forty-fifth day after the effective date thereof, unless prior thereto the successor shall, in accordance with such rules and regulations as the Commission may preserve, adopt such application as its own.

If any amendment to any application for registration pursuant to this subsection is filed prior to the effective date thereof, such amendment shall be deemed to have hern filed simultaneously with and as part of such application; except that the Commission may, if it appears necessary or appropriate in the public interest or for the protection of investors, defer the effective date of any such registration as thus amended until the thirtieth day after the filing of such amendment.

The Commission shall, after appropriate notice and opportunity for hearing, by order deny registration to or revoke the registration of any broker or dealer if it finds that such denial or revocation is in the public interest and that (1) such broker or dealer whether prior or subsequent to becoming such, or (2) any partner, officer, director, or branch manager or 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 willfully made or caused to be made In any application for registration pursuant to this subsection or in any document supplemental thereto or in any proceeding hefore the Commission with respect to registration pursuant to this subsection any statement which 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; or (B) has been convicted within ten years preceding the filing of any such application or at any time thereafter of any felony or inlademeanor involving the purchase or sale of any security of arising out of the conduct of the business of a broker or dealer; or (C) is permanently or temporarily enjoined by order, judgment, or decree of any court of competent jurisdiction from engaging mor continuing any conduct or practice in connection with the purchase or sale of any scenity; or (D) has willfully violated any provision of the Securities Act of 1933, as amended, or of this title, or of any rule or regulation thereunder. Pending final determination whether any such registration shall be denied, the Commission may by order postpone the effective date of such registration, for a period not to exceed fifteen days, but if, after appropriate notice and opportunity for heating, it shall appear to the Commission to be necessary or appropriate in the public interest or for the protection of investors to postpone the effective date of such registration until food determination, the Commission shall so order. Pending final determination whether any such registration shall be revoked, the Commission shall by order suspend such registration if, after

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* registered for the purposes of this section by putetion for registration, which shall contain to such broker or deuter and any person directly raded by, or under direct or indirect common et, as the Commission may by rules and regular tyrate in the public interest or for the protection of such application shall become effected such application by the Commission or within Commission may determine.

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coorists notice and opportunity for heating, tize the registration of any broker or deater vation is in the public interest and that (1) r of subsequent to becoming such, or (2) any : manager or such broker or dealer (or any ; performing similar functions), or any person controlled by such broker or dealer, whether E(A) has willfully made or caused to be marie regard to this subsection or in any document ceeding before the Commission with respect ection any statement which was at the time • coder which it was made false or misleading er (B) has been convicted within ten years estion or at any time thereafter of any felony use or sale of any scentity or arising out of x: or dealer; or (C) is permanently or tena or decree of any court of competent jurisf any conduct or practice in connection with : or (D) has willfully violated any provision nied, or of this title, or of any rule or regu-semination whether any such registration 7 order postpone the effective date of such Silteen days, but if, after appropriate notice sopear to the Commission to be necessary eller the protection of investors to postnone until final determination, the Commission Lation whether any such registration shall r order suspend such registration if, after

REGULATION OF OVER-THE-COUNTER MARKETS 13

appropriate notice and opportunity for hearing, such suspansion shall appear to the Commission to be necessary or appropriate in the public interest or for the protection of investors. Any registered broker or dealer may, upon such terms and conditions as the Commission may deem necessary in the public interest or for the protection of investors, withdraw from registration by filing a written notice of withdrawal with the Commission. If the Commission finds that any registered broker or dealer, or any broker or dealer for whom an application for registration is pending, is no longer in existence or has ceased to do business as 6 broker or dealer, the Commission shall by order cancet the registration of application of such broker or dealer.

 $\mathbf{E}(\mathbf{c})$ 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 scenarity fother than commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national scenarities exchange, by means of any manipulative, deceptive, or other frankelland 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 other francheut device) and regulations define such devices or contrivances as are manipulative, deceptive, or other such devices or other

(c) 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) atherwise than on a national securities exchange, in contrarentian of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors (1) to prevent fraudulent, deceptive, or manipulative acts or practices: (2) to prevent facilitious qualitanas: (3) to provide sofeguards with respect to the financial responsibility of brokers and dealers. (4) to regulate the manner, method, and place of soliciting business: and (5) to regulate the time and method of making selflements, payments, or deliveries: Provided, That nothing in clause (3), (4), or (5) of this subsection shall be construed to apply with respect to any transaction by a broker or dealer in any exempted scentify.

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(d) Each registration statement hereafter filed pursuant to the Securities Act of 1933, as amended, shall contain an undertaking by the issuer of the issueof scourities to which the registration statement relates to file with the Commission, in accordance with such tules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, such supplementary and periodic information, documents, and reports as may be required pursuant to section 13 of this title in respect of a security listed and registered on a national securities exchange; but such undertaking shall become overative only if the ageregate offering price of such issue of scourities, plus the agere-gate value of all other scourities of such issuer of the same class has hereinefter defined) outstanding, computed upon the basis of such offering price, amounts to \$2,000,000 or more. The issuer shall file such supplementary and periodic information, documents, and reports pursuant to such undertaking, except that the duty to file shall be untomatically suspended if and so long as (1) such issue of scentrities is listed and registered on a national scentities exchange, or (2) by reason of the listing and registration of any other scentity of such issuer on a national scentities exchange, such issuer is required to file pursuant to section 13 of this fitle information, documents, and reports substantially equivalent to such as would be required if such issue of securities were listed and registered on a national securities exchange, or (3) the aggregate value of all outstanding securities of the class to which such issue belongs is reduced to less than \$1,000,000. computed upon the basis of the effering price of the last issue of scentities of said class offered to the piddle. For the pitposes of this subsection, the term "class" shall be construed to include all securities of an issuer which are of substantially similar character and the holders of which enjoy substantially similar rights and privileges. Nothing in this subsection shall apply to scentifies issued by a foreign government or political subdivision thereof or to any other scentity which the Commission may by rules and regulations exempt as not comprehended within the purposes of this subsection.

SEC. 15.1. (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 additived sceneities association pursuant to subsection (b), under the terms and conditions hereinofter provided in this section, by filing with the Commission a registration statement in such form as the Commission may preserve, setting furth the information, and accompanied by the documents, before 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 thereta, and of its existing bylaws, and of any rules or instruments corresponding to the foregoing, whatever the name, hereingter 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 therewoder and to carry out the purposes of this section:

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 little 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 otherbise 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 specified basis relating to the type of business done by its members, or on such specified 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 of subsequent to becoming such, or (2) any partner, officer, director, or branch manager of such broker or dealer for any person occupying a similar status ar performing similar functions), or any person directly or indirectly controlling or controlled by such broker or dealer, whether prior or subsequent to becoming such, (c) has been and is suspended or expelled from a registered sceurities association (whether national or affiliated) or from a national sceurities exchange, for violation of any rule of such association or exchange which prohibits any acl 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 litle, 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 writer of the character described in clause (A) or (B) which is in effect with respect to such braker 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;

(8) 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 equilable principles of trute, to provide safeguards against unrensimable profits or unreasonable rates of commissions or other therpost, and, in general, to protect investors and the public interest, and to comove impediments to and perfect the unchanism of a free and open market; and are not designed to permit unfair discrimination between customers, or issuers, or brakers or dealers, to fix minimum profits, to impose any schedule of prices, or to impose any schedule or fix minimum rates of commissions, allowedges, discards, 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;

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men provide that, except with the approval or at the is cases in which the Commission finds it appropriate proce or direct, no broker or dealer shall be admitted in such association, if (1) such broker or dealer. is becoming such, or (2) any partner, officer, director, :-seer or dealer for any person accupying a similar - functions), or any person directly or indirectly run broker or dealer, whether prior or subsequent to est and is ruspended or expelled from a registered -- rational or affiliated) or from a national securities ry rule of such association or exchange which prohibits whiting conduct inconsistent with just and equitable ives any act the amission of which constitutes conduct splitable principles of trade, or (13) is subject to an *ying or revoking his registration pursuant to rection to suspending him from membership in a registered rational securities exchange, or (C) by his conduct ir, or directly or indirectly controlling or controlled s cause of any suspension, exputsion, or order of the 14 (.4) or (B) which is in effect with respect to such

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REGULATION OF OVER-THE-COUNTER MARKETS 15

(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 rates shall require that specific charges be brought; that such member shall be natified of, and be given an opportunity to defend against, such charges; that a record shall be kept; and that the determination shall include (1) 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, (11) a statement setting forth the specific rule or rules of the association of which any such act or practice, or unission 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 or lites, or the omission of any act required thereby, are deemed to constitute conduct incon-sistent 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 denied membership. 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 solisfied.

(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 additated securities association pursuant to subsection (d), to partici-pation in said applicant association as an additate 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 oscietation, 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 oplicated.

(e) Upon the filing of an application for registration pursuant to subsection (b) (c) Optic the piring of an appreciation for registration parsulation is subsection (d), ar subsection (d), the Commission shall by order grant such registration if the require-ments 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 parsonal to subsection (d) shall fail to be admitted promptly thereafter to affiliation with a registered national securities usual attion, the Commission shall revoke the registration of such appliated occurnies association.

(f) A registered scentilies association (whether national or appliated) may, upon such reasonable valies 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 widten where of withdrawal in such form as the Commission may by rules. and regulations preservice, but such withdrawed shall be subject to such appropriate terms and conditions for the orderly liquidation of such association as the Commis-sion may preserve. I pain the withdrawal of a mational accurities association from registration, the registration of any association applicated therewith shall automatically bermining.

(g) If any registered securities association (whether notional or appliated) shall take any disciplinary action against any member thereof, or shall dear admission to any broker or doube seeking membership there.a, such action shall be subject to review by the Commission, on its new motion, or upoh application by any person aggriceed 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 Cammission on its own motion, shall operate as a stay of such action until an order is issued upon such review pursuant to subsection (b).

(A) (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 consultration of the record before the association and such other coidence as it may derm relevant, shall (A) find that such member has engaged in such acts or practices, or has multical such use, as the association has found him to have engaged in or omitted, and (II) shall determine that such acts or practices, or omission to act, and 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 acts or practices, in accordance with paragraph (S) of this subsection. The Commission shall likewise determine whether the acts or practices prohibited, or the omission of any out required, by any such rule constitute conduct inconsistent with just and equivable principles of usariant 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 here in 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 here omitted is not required by such designated rule or rules, the Commission shall by order set aside the action of the association.

(8) 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 dismise 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.

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(1) (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.

(3) For the purposes of this subsection, the term "non-member 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 traduction in, or to induct the purchase or sale of, any security otherwise than on a mational 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 construct or applied as to present 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 scourities 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 inducest or for the protection of investors, copus 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, tak. They change in or addition to the rules of a consistent securities association shall take effect upon the thirtieth day after the filing of a copy three of with the Commission, ar upon such earlier date as the Commission may determine, unless the Commission shall rater and order unless such change or addition; and the Commission shall rater such an order unless such change or addition appears to the Commission to be consistent with the requirements of subsection (b) and subsection (b).

(k) (1) The Commission is authorized by order to abrogate any rule of a resistered securities association, if after appropriate notice and apportunity for maxing, 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 affairs or atherwise 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 ел 115-

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F OVER-TRE-COUNTER MARKETS

invation may determine. Application to the Comwith of review by the Commission on its own motion, is an until an order is issued upon such review pur-

ev disciplinary action taken by a registered scentilies "of, if the Commission, after appropriate notice and mederation of the record before the association and sem relevant, shall (.1) find that such member has ir has omitted such act, as the association has found 1. and (B) shall determine that such acts or practices, m of such rules of the association as have been desig-· substation, the Commission shall by order dismiss 26 ine Commission that such action should be modified " this enbecction. The Commission shall likewise Gos prohibiled, or the omission of any act required, # inconsistent with just and equitable principles of supers to the Commission that the evidence does not issue (A), or if the Commission shall determine that 15 to have been engaged in are not prohibited by the unistion, or that such act as is found to have been repeated rule or rules, the Commission shall by order

sud opportunity for hearing, the Commission finds number is excessive or oppressive, having due regard imm shall by order cancel, reduce, or require the

r ise denial of membership in a registered securities Cler appropriate notice and hearing, and upon the oscociation and such other endence as it may the specific grounds on which such denial is based is section, the Commission shall by order dismiss mission shall by order set aside the action of the such applicant broker or dealer to membership

rearilies association may provide that an member near broker or dealer (as defined in paragraph (2) to prices, for the same commissions or fers, and on are by such member accorded to the general public, witton, the term "non-member broker or dealer" shall makes use of the marks or of any means or instrueffect any transaction in, or to induce the purrease than on a national securities exchange, who instructs association, except a broker or dealer who ter, bankers' acceptances, or commercial bills.

that be so construct or applied as to prevent any invitation from granting to any other member of thy dealer's discount, allowance, commission, or

inclution shall file with the Commission in accordts as the Commission may preserve as necessary π is for the protection of twestors, copies of any π of the ossociation, and such other information may require to keep current or to supplement the infield pursuant to subsection, (a). Any change second securities association shall take effect upon z way thereof with the Commission, or upon such itermine, unless the Commission shall enter an idition: and the Commission shall enter such Elin appears to the Commission to be consistent is and subsection (d).

rest by order to abrogate any rule of a registered reseate notice and apportunity for hearing, it is throgation is accessary or appropriate to assure usociation, to assure a fair representation of its ifairs or otherwise to protect investors or effectu-

239 request any registered securities association is supplement to its rules with respect to any of

REGULATION OF OVER-THE-COUNTER MARKETS 17

the matters hereinafter enumerated. If such association fails to adopt such alteration as 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 horizing, it appears to the Commission that such alteration or supplement is accessary or appropriate in the public interest or for the protection of invalors or to effect and the purposes of this section, with respect to $\{1\}$. The basis for, and providers 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 afficers and directors; and (4) affiliation between registered securities associations.

(1) 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 corry out the purposes of this section—

(1) after appropriate notice and opportunity for henring, by order to suspend for a period not exceeding lively emotiles 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 actu rules, or has engaged in any other octivity tending to defeat the purposes of this section:

(3) after appropriate notice and apportunity for hearing, by order to suspend for a period not exceeding lucies months or to expel from a registered securities association any member thereof who the Commission finits (1) has violated any provision of this title or any rule or regulation thereunder, or has effected any iransaction 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 Actof 1935, 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 wilfully 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.

(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. 17. (a) Every national scentitics exchange, every member thereof, [every broker or dealer who transacts a business in scentifies through the medium of any such member,] *every registered scentifies association*, and every broker or dealer registered parsuant to section 15 of this title, shall make, keep, and preserve for such periods, such accounts, correspondence, memoranda, papers, books, and other records, and make such reports, as the Commission by its rules and regulations may proscribe as necessary or appropriate in the public interest or for the protection of investors. Such accounts, correspondence, memoranda, papers, books, and other records shall be subject at any time or from time to time to such reasonable periodic, special, or other examinations by examiners or other representatives of the Commission as the Commission may deem necessary or appropriate in the public interest or for the protection of investors.

(b) Any broker, dealer, or other person extending credit who is subject to the rules and regulations prescribed by the Federal Reserve Board pursuant to this title shall make such reports to the Board as it may require as accessary or appropriate to enable it to perform the functions conferred upon it by this title. If any such broker, dealer, or other person shall fail to make any such report or fail to furnish full information therein, or, if in the judge cut of the Phard it is otherwise pecessary, such broker, dealer, or other person shall permit such inspections to be made by the board with respect to the business operations of such broker, dealer, or other person shall permit such inspections to be made by the Board with respect to the business operations of such broker, dealer, or other person as the Board may deem necessary to enable it to obtain the required information.

SEC. 29. (a) Any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or of any rule or regulation thereander, or of any rule of an exchange required thereby shall be void.

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(b) Every contract made in violation of any provision of this title or of any rule or regulation theremuler, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter mode the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this title or any rule or regulation thereander, shall be vaid (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule or [regulation.] regulation Provided. That no contract shall he void by reason of this subsection because of any violation of any rule or regulation prescribed parament to clause (3), (4), or (3) of subsection (c) of section 15 of this title, except insolar as the Commission, having determined that such action is necessary or appropriate for the protection of investors, shall have expressivy provided in such rule or regulation that the protections of this subsection shall apply in the case of any violation thereof. (c) Nothing in this title shall be construed (1) to affect the validity of any

(c) Nothing in this title shall be construed (1) to affect the validity of any loan or extension of credit (or any extension or renewal thereof) made or of any lien created prior or subsequent to the enactment of this title, unless at the time of the making of such loan or extension of credit (or extension or renewal thereof) or the creating of such lien, the person making such loan or extension of credit (or extension or renewal thereof) or acquiring such lien shall have actual knowledge of facts by reason of which the making of such loan or extension of credit (or extension or renewal thereof) or the sequisition of such lien is a violation of the provisions of this title or any rule or regulation thereander, or (2) to afford a defense to the collection of any debt or obligation or the enforcement of any lien by any person who shall have acquired such debt, obligation, or lien in good faith for value and without actual knowledge of the violation of any provision of this title or any rule or regulation thereing the legality of such debt, obligation, or lien.

Sec. 32. (a) Any person who willfully violates any provision of this title, or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the $t_{\rm c}$ and of this title, or any person who willfully and knowingly makes, or causes to be made, any statement in any application, report, or document required to be filed under this title or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 15 of this title, which statement was false or mislending with respect to any material fact, shall upon conviction be fined not more than S10,000, or imprisoned not more than two years, or both, except that when such person is an exchange, a fine not exceeding \$500,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

(b) Any issuer which fails to file information, documents, or reports pursuant to an undertaking contained in a registration statement as provided in subsection (d) of section 15 of this title shall forfeit to the United States the sum of S100 for each and every day such failure to file shall continue. Such forfeiture, which shall be in lieu of any criminal penalty for such failure to file which might be deemed to arise under subsection (a) of this section, shall be payable into the Treasure of the United States and shall be recoverable in a civil suit in the name of the United States.

(c) The provisions of this section shall not apply in the case of any violation of any rule or regulation prescribed pursuant to clause (3), (4), or (5) 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 filled 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.

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