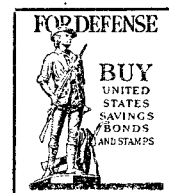


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N.A.S.D. NEWS

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Volume II

Washington, D. C., February 15, 1942

Number 4

Executive Director's Report For 1941 Covers Enforcement Program Results

Fulton Finds Only 5 per cent of Members Seriously Violated Rules

Nearly 1,000 of the 2,900 members of the National Association of Securities Dealers have been examined by the Association and it was necessary in 1941 to file but 120 so-called formal complaints against members for violations of the Rules of Fair Practice, Wallace H. Fulton, Executive Director, told the Board of Governors at its meeting January 15.

Mr. Fulton pointed out that all complaints were not based upon serious abuses of the principles of the business or the Rules of the Association and that, as a matter of fact, but 5 or 6 per cent of the complaints lodged against members last year involved seriously objectionable practices. The record is a cause for deep satisfaction of the membership, Mr. Fulton added.

"We have talked about the 'fringe' but we have not always been certain how wide an area of the whole cloth would be covered by the 'fringe.' We know now that it is not large and not beyond our surveillance."

Following are extracts from the official report of the Executive Director to the Board:

Trade Practice Complaints

I would like to discuss details of the origin and disposition of trade practice complaints for the year 1941. The data for 1941 show that 120 formal complaints were lodged against members during the year. In 1940, 20 formal complaints were filed while in 1939 there were 2. The simple contrasting of those
(Turn to Page 3, Column 1)

District Committees

A list of members of the fourteen District Committees of NASD appears on pages 2 and 4.

OFFICERS FOR 1942

CHAIRMAN

H. H. Dewar, Dewar, Robertson & Pancoast, San Antonio, Tex.

VICE CHAIRMAN

Lee M. Limbert, Blyth & Co., Inc., New York, N. Y.

VICE CHAIRMAN

Francis F. Patton, A. G. Becker & Co., Incorporated, Chicago.

TREASURER

Robert W. Baird, The Wisconsin Company, Milwaukee, Wis.

EXECUTIVE DIRECTOR

Wallace H. Fulton, Washington, D. C.

EXECUTIVE COMMITTEE

Messrs. Dewar, Limbert, Patton, Baird

Hermann F. Clarke, Estabrook & Co., Boston, Mass.

Mark C. Elworthy, Elworthy & Co., San Francisco.

Laurence M. Marks, Laurence M. Marks & Co., New York.

Wallace H. Fulton (ex-officio).

FINANCE COMMITTEE

William A. Fuller, Chairman, Fuller Cruttenden & Company, Chicago.

Messrs. Baird and Dewar

F. Edward Bosson, Putnam & Co., Hartford, Conn.

Wallace H. Fulton (ex-officio).

Securities Industry Unites Behind Treasury War Program

Investment bankers, securities dealers and brokers, through their national associations, have united as a volunteer unit to promote the sale of Defense Bonds and Tax Savings Notes being issued by the Treasury Department to finance the war.

Officers of the National Association of Securities Dealers were instrumental in initiating the cooperative program.

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Dewar Elected Chairman; Texan Succeeds Baird; Plans Continuing Program

"Best Interests of Business" Always Major Consideration In Forming Policy

H. H. ("Hal") Dewar of San Antonio, Texas, is NASD Chairman for 1942. He was elected at a meeting of the Board of Governors January 16 in New York City. His firm is Dewar, Robertson & Pancoast, organized in 1932.

Mr. Dewar succeeds Robert W. Baird of Milwaukee, Wis., who served during 1941. Mr. Baird is president of The Wisconsin Company.

The new Chairman will be 40 in March. He was born in Chicago. He is a graduate of Texas University. After leaving college in 1923, Mr. Dewar joined the Guaranty Company of New York. From 1924 to 1929, he was associated with J. E. Jarratt Company, San Antonio and from 1929 to 1931 was manager of the bond department of the Alamo National Company, also of San Antonio. After serving as Chairman of the Texas District of the Investment Bankers Conference for two years, he became a Governor of NASD in 1940.

Not Accepted Lightly

"It is an honor which one cannot accept lightly," Mr. Dewar said upon his election. "Bob" Baird and all the members of the Board did an excellent job in 1941. It is my hope that I will be able to carry on, with the help of the present Board, the constructive pro-

(Turn to Page 7, Column 3)

Advisory Council, Secretaries Meet in New York Feb. 3-5

A meeting of the Advisory Council, consisting of Chairmen of the fourteen District Committees and all District Secretaries, will be held in New York, February 3-5, inclusive. The meetings will be devoted to discussions of Association activities past, present and future, permitting a free exchange of experiences of the Association's staffs during the past year.

District Committee Personnel, Chairmen Elected In Fourteen NASD Areas

Groups Are Administrative Agencies In Charge of District Association Business

Formation of District Committees and the election of Chairmen and other District officers for 1942 has been completed in the fourteen NASD districts. These District Committees are the ranking administrative agencies of the Association in their areas. Upon them rests the duty of administering the affairs of their Districts in all details of Association business—Business Conduct, Quotations, Uniform Practice, etc. In many Districts, the District Committee acts as the area's Business Conduct Committee.

Following is a list of members of all District Committees, the Chairmen of which will serve until January, 1943:

(District No. 1)

(Idaho, Ore., Wash.)

Richard H. Martin (Chrm.)
Ferris & Hardgrove
Portland, Ore.

Archibald W. Talbot (V. Chrm.)
Hartley, Rogers & Company
Seattle, Wash.

Beardslee B. Merrill (Sec'y.)
Richards & Blum, Inc.
Spokane, Wash.

Frank A. Bosch
Warrens, Bosch & Floan
Portland, Ore.

Waldo Hemphill
Waldo Hemphill & Co.
Seattle, Wash.

George R. Yancey
Murphey, Favre & Co.
Spokane, Wash.

District No. 2

(California)

North

(San Francisco)

Roy L. Shurtleff (Chrm.)
Blyth & Co., Inc.

H. R. Baker
H. R. Baker & Co.

Spencer Brush
Brush, Slocumb & Co.

Thomas M. Hess
Gibbons & Hess

Norman D. Weeden
Weeden & Co.

South

(Los Angeles)

Ralph E. Phillips (V. Chm.)
Dean Witter & Co.

Warren H. Crowell
Crowell, Weedon & Co.

Colis Mitchum
Mitchum, Tully & Co.

Donald O'Melveny
O'Melveny-Wagenseller & Durst

Charles F. Sill
M. H. Lewis & Company

A. S. Van Denburgh, Jr.
Van Denburgh & Bruce, Inc.

District No. 3

(Ariz., Colo., N. M., U., Wyo.)

(Denver unless otherwise indicated)

Jerry C. Vasconcells (Chrm.)
Vasconcells, Hicks & Co.

Malcolm F. Roberts (V. Chrm.)
Sidlo, Simons, Roberts & Co.

Arthur H. Bosworth
Bosworth, Chanute, Loughridge & Co.

Donald F. Brown
Donald F. Brown & Co.

Edward B. Coughlin
Coughlin and Company

Robert D. Sims
Sims, Newman and Co.
Colorado Springs, Colo.

Paul E. Youmans
Sullivan & Company

District No. 4

(Minn., Mont., N. D., S. D.)

Norman Nelson (Chrm.)
Piper, Jaffray & Hopwood
Minneapolis, Minn.

Wilber W. Wittenberg (Sec'y.)
Wittenberg Merrick Company
Minneapolis, Minn.

Homer Collins
Homer Collins & Company
Duluth, Minn.

Stanley Gates
Stanley Gates & Co.
St. Paul, Minn.

Almon A. Greenman
Greenman & Cook, Inc.
St. Paul, Minn.

Dewey F. Gruenhagen
Thrall West Company
Minneapolis, Minn.

William Mannheimer
Mannheimer-Caldwell, Inc.
St. Paul, Minn.

Clyde C. Needham
Needham & Company, Inc.
Minneapolis, Minn.

Elmer L. Williams
Allison-Williams Company
Minneapolis, Minn.

District No. 5

(Kans., West Missouri, Okla.)

Harlan Herrick (Chrm.)
The Lathrop-Hawk-Herrick Company
Wichita, Kansas

Howard H. Fitch (V. Chrm.)
Stern Brothers & Co.
Kansas City, Mo.

George K. Baum
Baum, Bernheimer Company
Kansas City, Mo.

Harry A. Beecroft
Beecroft, Cole & Company
Topeka, Kansas

G. H. C. Green
R. J. Edwards, Inc.
Oklahoma City, Okla.

Eugene L. Young
Kansas City, Mo.

District No. 6

(Texas)

Wm. P. Smallwood (Chrm.)
The State Investment Company
Fort Worth, Texas

Jack P. Brown
Dallas Union Trust Company
Dallas, Texas

Elmer A. Dittmar
Mahan, Dittmar & Company
San Antonio, Texas

Donald D. James
E. J. Roe and Company
San Antonio, Texas

Robert E. Moroney
Moroney, Beissner & Co.
Houston, Texas

J. L. Mosle
Mosle and Moreland
Galveston, Texas

District No. 7

(Ark., East Mo., Ky.)

(St. Louis unless otherwise indicated)

Joseph G. Petersen (Chrm.)
Eckhardt-Petersen and Co., Inc.

John D. McCutcheon (V. Chrm.)
John D. McCutcheon and Co., Inc.

Firmin D. Fusz, Jr.
Fusz-Schmelzle & Co.

A. B. Tilghman
A. G. Edwards & Sons

J. R. Vinson
J. R. Vinson and Company, Incorporated
Little Rock, Ark.

James C. Ward
G. H. Walker & Co.

Louis J. Nicolaus
Stifel, Nicolaus & Company, Inc.

District No. 8

(Ill., Ind., Ia., Mich., Nebr., Wis.)

Paul S. Grant (Chrm.)
The Milwaukee Company
Milwaukee, Wis.

Howard F. Allen (V. Chrm.)
Central Republic Company
Chicago, Ill.

L. Raymond Billett
Stern, Wampler & Co., Inc.
Chicago, Ill.

(Turn to Page 4, Column 1)

EXECUTIVE DIRECTOR'S REPORT FOR YEAR 1941

(Continued from Page 1)

figures tells more than any words I could muster in order to describe the change that has taken place in a period of a year. And for the present I am counting only the so-called formal complaints.

The figures on formal complaints received in 1941 do not tell the whole story for it will be appreciated that the April, 1941, meeting of the Board supplied the enforcement program with a forceful impetus. The statistics make this plainly evident. In the first four months of the year, 12 formal complaints were filed against the membership, an average of three per month. In the succeeding nine months, 108 formal complaints were filed, an average of 12 per month. Even this evidence of an accelerated pace is not too exact a picture because the momentum of the program took several months to produce the peaks finally reached. In November, 25 formal complaints were filed and in December 15. It is neither my purpose nor desire to anticipate future events, but for a while longer, it now appears, we may expect an approximation of the most recent months to prevail. Several Districts got their enforcement programs under way late in the year and the results in these cases have not had opportunity to find reflection in the 1941 compilation.

75 Disposed Of

Of the 120 complaints filed during the year, and those carried over from 1940, District Business Conduct Committees disposed of 75, leaving 48 pending. Many of these required several meetings of the Committees, with numerous hearings being held, at which the member respondent appeared alone or with counsel. Such hearings often took several hours with testimony and pleadings comparable to a court of law although of course on a much more informal basis. (It is our purpose to make such hearings as free as possible of strict legal construction but to employ reasonable judicial processes to the end that all parties are heard and the record, upon which findings are made, is complete.)

Deliberations by the Business Conduct Committees, whether or not hearings were held, resulted in the disposition of the 75 cases closed during the year as follows: expulsions 26; suspensions 6; fines 29 (these ranging from \$36 to \$1500); censures 32; dismissals or withdrawals 6. Ten cases came be-

NASD Policy On Unlisted Applications

The Association in November appeared before the SEC as a party in opposition to applications of the New York Curb Exchange to extend unlisted trading privileges to three issues of utility bonds being traded in over-the-counter markets. The Executive Committee decided that the Association should intervene in these applications because a large body of our membership had an interest in seeing that these issues were retained for over-the-counter trading. One hearing on the applications was held before a trial examiner. At the request of the New York Curb Exchange, further hearings on the applications were adjourned, Counsel for the Curb basing his plea for an adjournment on the volume and character of the evidence presented by Mr. Hanson for the NASD. Further hearings on these applications were scheduled to be held this month.

NASD intervention in these applications marks a new departure in Association activities. It is the feeling of the Executive Committee that the Association should, in the future, examine all applications made by Exchanges seeking to extend unlisted trading privileges to securities being traded over-the-counter. Where such action is warranted by the circumstances surrounding the issues involved, the Association, in the name of its members, will oppose the granting to the Exchanges of such unlisted trading privileges. This does not mean, necessarily, that the Association will oppose all applications of this kind, but it does mean that each such application will be studied and, when deemed appropriate for the interests of the members, and the investor, the application will be opposed.—Extract from report of Executive Director to Board of Governors.

fore the National Business Conduct Committee on appeal or review.

These statistics tell an important story. They mean that the Association intends to police its members and is capable of so doing; further, that it

will discipline members according to the degree of abuse in which they are proven to have indulged.

Consider that this Association has about 2,900 members and reflect that nearly 1,000 have been reached by our examining processes to date. Is there not cause for satisfaction that, in view of those facts, the Association found cause in 1941 to file complaints against but 120 of the large number examined? We have talked about "the fringe" but we have not always been certain how wide an area of the whole cloth would be covered by the fringe. We know now that it is not large and not beyond our surveillance. The relationship of complaints to members examined does not in any sense mean that this proportion of the membership engaged in serious abuses of the principles of this business and the Rules of the Association. As a matter of fact, not more than 5 or 6 per cent of the complaints involved violations of a seriously objectionable nature. About half of them were attributable to negligence, ignorance or habits which short-cut the letter of the law and the Rules; or to financial difficulties for which the times, as much as any other cause, were responsible. I feel we can be confident that the disciplinary action taken against such departures has had the effect of permanently correcting the cause for the complaints.

Practically all complaints against members contained charges of violation of Section 1 of the Rules of Fair Practice which is the section requiring that members observe high standards of commercial honor and just and equitable principles of trade. Any departure from the Rules is almost automatically a violation of this principle of the business. The other most common violation was of Section 4 which says that a member must charge fair prices and reasonable commissions. Next, as a source for complaints, were violations of Rule 18 which is the manipulative, fraudulent and deceptive devices—section under which secret profits and other parallel improper acts may be charged. Next in the order of importance as a cause for complaints were improper disclosures in confirmations; next, improper recommendations to customers, and then violations of commingling and hypothecation rules. Several complaints included charges of failure to maintain and preserve proper books and records and in a few instances complaints were filed for re-

(Turn to Page 5, Column 1)

District Committee Personnel—*(Continued from Page 2)*

Louis J. Cross
Paul H. Davis & Co.
Chicago, Ill.

Charles B. Crouse
Crouse & Company
Detroit, Mich.

Michael D. Dearth
Murdoch, Dearth & White, Incorporated
Des Moines, Iowa

Noah M. Dixon
The Dixon-Bretscher Company, Inc.
Springfield, Ill.

Walter E. Kistner
A. C. Allyn and Company
Chicago, Ill.

Augustus Knight
Knight, Dickinson & Co.
Chicago, Ill.

Bennett S. Martin
The First Trust Company of Lincoln,
Nebr.
Lincoln, Nebr.

G. William Raffensperger
Raffensperger, Hughes & Co., Inc.
Indianapolis, Ind.

William C. Roney
Wm. C. Roney & Co.
Detroit, Mich.

District No. 9
(Ala., Fla., Ga., La., Miss., S. C., Tenn.)

Clement A. Evans (Chrm.)
Clement A. Evans & Company
Atlanta, Ga.

Brownlee O. Currey (V. Chrm.)
Equitable Securities Corporation
Nashville, Tenn.

Julian R. Hirshberg
Norris & Hirshberg, Inc.
Atlanta, Ga.

D. J. Lucas
G. H. Crawford Co., Inc.
Columbia, S. C.

Porter King (Sec'y.)
King, Mohr and Company
Mobile, Ala.

Henry J. Blackford
A. M. Law & Company
Spartanburg, S. C.

Francis B. Childress
Childress and Company
Jacksonville, Fla.

Jo Gibson, Jr.
Webster & Gibson
Nashville, Tenn.

John B. Shober
Woolfolk Huggins & Shober
New Orleans, La.

J. Mills Thornton
Montgomery, Ala.

Macrery B. Wheeler
Wheeler & Woolfolk, Incorporated
New Orleans, La.

District No. 10
(Ohio, Louisville, Lexington, Ky.)

Peter Ball (Chrm.)
Ball, Coons & Company
Cleveland, Ohio

Ray M. Brock
Greene & Brock
Dayton, Ohio

Harry E. Collin
Collin, Norton & Co.
Toledo, Ohio

Roderick A. Gillis
Gillis, Russell & Co.
Cleveland, Ohio

George T. Lennon
George T. Lennon & Company
Columbus, Ohio

Robert J. McBryde
James C. Willson & Co.
Louisville, Ky.

Neil Ransick
Charles A. Hirsch & Company, Inc.
Cincinnati, Ohio

Arthur S. Sedley
The Bankers Bond Co.
Louisville, Ky.

District No. 11

(Dist. of Col., Md., N. C., Va., W. Va.)

Howard E. Demuth (Chrm.)
Mackubin, Legg & Company
Baltimore, Md.

L. Gordon Miller (V. Chrm.)
Miller & Patterson
Richmond, Va.

Oscar Burnett
Oscar Burnett and Company, Inc.
Greensboro, N. C.

James Parker Nolan
Folger, Nolan & Co., Inc.
Washington, D. C.

Harold C. Patterson
Auchincloss, Parker & Redpath
Washington, D. C.

Harry R. Piet, Jr.
John D. Howard & Co.
Baltimore, Md.

District No. 12

(Delaware & Pennsylvania)

Pittsburgh

Nathan K. Parker (Chrm.)
Kay, Richards & Company

Joseph Buffington, Jr.
Young & Co., Inc.

Ernest O. Dorbritz
Moore, Leonard & Lynch

S. Davidson Herron
Mellon Securities Corporation

Robert C. Schmertz
Phillips, Schmertz & Co.

Philadelphia

William K. Barclay, Jr. (V. Chrm.)
Stein Bros. & Boyce

John C. Bogan, Jr.
Sheridan, Bogan Co.

Robert G. Rowe
Stroud & Company, Incorporated

E. C. Sayers
Smith, Barney & Co.

David S. Soliday
Hopper, Soliday & Co.

District No. 13
(Conn., N. J., N. Y.)

Henry G. Riter, 3rd (Chrm.)
Riter & Co.
New York, N. Y.

Irving D. Fish (V. Chrm.)
Smith, Barney & Co.
New York, N. Y.

Russell V. Adams
Adams & Mueller
Newark, N. J.

Harry W. Beebe
Harriman, Ripley & Co., Incorporated
New York, N. Y.

Robert C. Common
Vietor, Common & Company
Buffalo, N. Y.

George R. Cooley
George R. Cooley & Co., Inc.
Albany, N. Y.

Frank Dunne
Dunne & Co.
New York, N. Y.

Gail Golliday
Bonbright & Company, Incorporated
New York, N. Y.

Charles F. Hazelwood
E. H. Rollins & Sons, Incorporated
New York, N. Y.

Robert S. Morris
Robert S. Morris & Company
Hartford, Conn.

Richard C. Rice
J. K. Rice, Jr. & Co.
New York, N. Y.

Meyer Willett
Bristol & Willett
New York, N. Y.

District No. 14

(Maine, Mass., N. H., R. I., Vt.)

Lester Watson (Chrm.)
Hayden, Stone & Co.
Boston, Mass.

Alvah R. Boynton
F. S. Moseley & Co.
Boston, Mass.

Ralph F. Carr
Ralph F. Carr & Co.
Boston, Mass.

Albert H. Poland
Miller & George
Providence, R. I.

Roger B. Ray
Portland, Maine

Thomas A. West
Perrin, West & Winslow, Inc.
Boston, Mass.

Max O. Whiting
Whiting, Weeks & Stubbs, Inc.
Boston, Mass.

Executive Director's Report—

(Continued from Page 3)

fusal by the member to permit accredited NASD representatives to inspect books and records.

Minor infractions of Rules which result in communications from District Committees are, for technical purposes of the record, identified as informal complaints. In 1941, 137 such instances occurred. Because of the thoroughness of such examinations, the largest proportion of these grew out of the mass examinations in Districts 3 and 4. In the former, 39 instructional letters were written to members calling attention to the fact that certain of their practices with respect to confirmation disclosures, manner of hypothecation of customers' securities and other rules, such as those respecting books and records, were not in conformity with Association rules or accepted standards of sound business practice. In the case of District No. 4, 36 similar letters were employed. The majority thus contacted expressed appreciation for the counsel supplied them and all said they were correcting the causes for the letter of instruction. However, a number of members receiving such communications from their District Committees resented what they considered was excessive exercise of Association authority. A few felt that their reputations and their integrity had been assailed unwarrantedly. There was also criticism of articles in the NEWS discussing the general nature of these violations. The letters of instruction from the District Committees and the articles in the NEWS were, of course, purely educational in purpose. They were in no wise inspired by a desire to cast reflections upon the character or integrity of any member but, on the contrary, were intended to be of constructive service to the individual member and the membership at large. When a member is conducting his business with conscientious regard for the high principles of the business but unwittingly or unknowingly is deficient in one or more of the technical requirements, we conceive that we owe it to that member to call such deficiencies to his attention. Should we fail in this, the failure would be a serious reflection upon us. At least, that is our concept of our duty.

Analysis of the year's record of informal complaints shows that 28 of the total were filed in the first four months of the year, an average of 7 per month. Excluding the number filed in Districts Nos. 3 and 4, informal complaints in the last eight months of the year to-

Membership of Association Declined Slightly in 1941

The Association closed the year 1941 with 2,883 members. At the end of 1940 the membership numbered 2,899. Thus, despite the difficulties encountered by the business during the past year, the total membership suffered only a slight reduction. It is interesting to note the source of membership terminations. In the last four months of the year, for example, the Association lost 127 members either by retirement from business or other causes. Eighty-five of that total or 66 per cent were class 1 members—those with fewer than 4 persons employed in securities activity. Twenty additional terminations were in class 2—members with fewer than 7 employed in securities activity. Eighty-two per cent of the members withdrawing from the Association were, therefore, of the smallest size measured by dues-paying classification. Three "occasional underwriters"—accounting for annual underwriting of from \$1,100,000.00 to \$3,000,000.00—withdrawed from membership in the period under review.—Extract from report of Executive Director to Board of Governors.

talled 34, an average of 4 per month. When these statistics are related to those for formal complaints, it will be seen that District Business Conduct Committees are not treating lightly incoming evidences of Rule violations.

Examinations

Several methods of examining members have been employed in the various Districts. Seven of the Districts employed the District Secretaries in the making of routine examinations and in pursuit of specific complaints; three Districts have employed questionnaires on a District-wide scale or in important centers of the District, with follow-up checks being made in some instances by CPA's; two Districts have sponsored mass examinations of the membership with Association examiners and Secretaries; one District has employed a local firm of CPA's to examine members in their turn. Finally, the California District has, in the northern sec-

tion, employed a questionnaire and, in the Southern District, has been engaged in routine examinations by an employed examiner who has completed 30 out of 112.

Thus every District, in one manner or another, has undertaken or completed examinations of its members.

The mass examinations referred to were conducted in No. 3 and No. 4—the Minnesota and the Denver Districts. All members of those Districts were reached in these examinations. In Nos. 6 and 9—Texas and the South, respectively—the memberships were blanketed with an exhaustive questionnaire-form designed to establish financial character and business practice policies. In the New York District numerous examinations have been conducted where they seem dictated by information or circumstances known to the District and toward the end of the year the District was completing a questionnaire form which was to be sent to all its 1,000 members. In District No. 14 (New England), 34 members of the 254 total in the District were examined by an accounting firm.

In the remainder of the Districts, examinations have been conducted mostly by the District Secretaries and here is how we stand in those areas:

In No. 1 (Idaho, Oregon and Washington) 43 of the 85 have been reached; in No. 5 (Kansas, West Missouri and Oklahoma) 13 of the 53 members have been examined; in No. 7 (East Missouri), 48 of the 71; in No. 8, 194 in Chicago and Indianapolis have been questionnaire-examined and reviewed by an accounting firm, of a District-wide total of 431; in No. 10 (Louisville and Lexington, Ky. and all of Ohio) 41 examinations have been completed of 130 members; in No. 11 (the District of Columbia area) 22 of the 128 members have been examined; in No. 12 (Pennsylvania), 29 of the 209 have been examined.

The two mass examinations conducted by District and Washington staff people naturally took a number of the examining force away from their normal duties for weeks at a time. Otherwise, the examinations made by District Secretaries would be even further along than they are but in making that observation, I am in no wise understating progress of the Secretaries in their District work. Before very many months have passed, every member of this Association, it is hoped, will have submitted to one or another form of review of his financial position and policies. No such thorough-going study

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of the investment banking and securities business ever before was undertaken or accomplished. Opposition to this program on the part of individual members has been rare.

Examination Methods and Costs

As previously set forth, three methods were employed in large scale examinations of members—so-called mass examinations by staff people; questionnaire-examinations in District No. 8 with follow-ups by the accounting firm in charge; continuous spot examinations by a firm of certified public accountants. Each of these methods has its advantages and disadvantages from the standpoint of results and costs insofar as these can be established at present.

While mass-examinations appear to be the least expensive process, they have obvious disadvantages. Foremost of these is the fact that when five or six staff examiners and Secretaries conduct such examinations away from their home offices they are completely divorced from their normal duties for periods of two or three weeks while engaged in the field and another week or two must be devoted by them in preparation of their reports when they return to their offices. The effectiveness of such examinations must, therefore, be weighed against the loss of these men from their normal duties for prolonged periods.

Because of incomplete cost figures it is impossible at this time to make any recommendations to the Board as to the most satisfactory method of proceeding with examinations on the scale discussed. At the next meeting of the Board it will be possible to review this subject more exactly.

Organization

As the review of enforcement activities will suggest, the field organization has undergone some expansion since the January, 1941, report to the Board. During the year 1940—devoted, as it was, largely to organizational and educational efforts—only the largest of the fourteen Districts found it necessary to employ full-time administrative personnel. A year ago, therefore, there were six Secretaries serving as many Districts—New York, Chicago, San Francisco, Los Angeles, Boston and Columbus. In the remainder of the Districts, the District Chairmen with, in some instances, part-time assistance, discharged all administrative duties of

NASD OBJECTIVES

To promote through cooperative effort the investment banking and securities business, to standardize its principles and practices, to promote therein high standards of commercial honor, and to encourage and promote among members observance of Federal and State securities laws;

* * *

To provide a medium through which its membership may be enabled to confer, consult, and cooperate with governmental and other agencies in the solution of problems affecting investors, the public and the investment banking and securities business;

* * *

To adopt, administer and enforce rules of fair practice and rules to prevent fraudulent and manipulative acts and practices, and in general to promote just and equitable principles of trade for the protection of investors;

* * *

To promote self-discipline among members, and to investigate and adjust grievances between the public and members and between members.—Extracts from the Certificate of Incorporation.

the District. As these multiplied and became more demanding as to scope and time, several other Districts recognized the need for full-time, trained personnel. As a result, at the end of 1941, instead of six, the Association had ten District Secretaries and the New York office an assistant secretary, as well, who devotes one-half of his time to the duties of Secretary of the Uniform Practice Committee. Three other Districts, as the year closed, employed part-time assistants to the Chairman; in another, no paid personnel was employed. One of these has under consideration the employment of a full-time secretary; another has steadily increased the amount of work assigned to the part-time secretary until he is now practically on a full-time basis.

In addition, the expanded enforcement work made it necessary for the larger Districts to employ trained examiners. New York has four examiners on its staff; Chicago, two, and Los Angeles, one. Other Districts, but for assistance rendered by the Washington staff and contemporary personnel,

would have found it necessary last year to engage examiners as regular or temporary employees. Use of local certified public accounting firms also was instrumental in making staff District examiners unnecessary. (I will discuss details of these examination methods in another section.)

Our District organizations have an excellent record of performance in a year full of new problems and ever-growing demands. District forces, as a whole, have worked hard and long at their tasks, and it is to their credit that the Association can look back upon a year of real accomplishment.

Dunne Advocates New Unlisted "Yardsticks" At House Hearings

Granting of unlisted trading privileges to applicant stock exchanges should be based upon the "prospective trading activity" of the issue when admitted and its retention on the exchange should be dependent upon periodic investigation of the actual volume of trading being done on the exchange.

Frank Dunne, Dunne & Co., New York City, suggested this yardstick to the House Interstate and Foreign Commerce Committee when Mr. Dunne appeared as a witness in the Committee's hearings on amendments to the Securities Exchange Act. Mr. Dunne is a retiring Governor of NASD and is currently serving on District Committee #13. He is also president of the New York Security Dealers Association.

"Vague" yardsticks, (such as the volume of activity in the "vicinity" of the exchange) which are now in use, are not effective guides for the solution of this important problem, Mr. Dunne said. Differentiating between the techniques of trading in an "auction" and a "dealer market," Mr. Dunne contended that the former cannot be successfully employed for securities having the following characteristics: (1) lack of speculative interest; (2) small capitalization; (3) limited distribution; (4) high price; (5) desirability for portfolios of institutions, such as insurance companies. Institutions, he said, "often wish to negotiate on a sizable block at one price" and execution is only possible through the cooperative efforts of numerous dealers.

Backbone of Business

The witness made it clear that he did not oppose exchange trading, as such. (Continued on Page 7, Column 2)

State Securities Commissioners Favor Continued Cooperation With NASD; Selby Elevated

Ohio Securities Chief Made President of NASC; Zeller Heads Cooperating Group

The program of cooperation between the NASD and the National Association of Securities Commissioners was furthered at the recent convention of the Commissioners at which Paul L. Selby, former chairman of the NASC cooperative committee, was elected president of NASC. Mr. Selby is the Chief of the State Division of Securities in Ohio.

As successor to Mr. Selby as chairman of the NASC cooperative committee, Vern G. Zeller, Director, Department of Securities of Wisconsin, was chosen. Mr. Zeller has been directing efforts of the NASC to draft a standard registration form. This work is being combined with a broader program now to be fully directed by Mr. Zeller.

In retiring as chairman of the Committee on Cooperation of NASC, Mr. Selby submitted a report to the convention recommending continuation of the program and advising of excellent success in the work to date. Mr. Selby outlined eight objects of the work including uniformity in procedural matters, vigorous enforcement of laws against sub-marginal operators, relief from "rigorous registration requirements for sound legitimate security issues and legitimate security dealers," more interest in the legitimate licensed security dealers and less emphasis upon the illegal operations with the idea of educating the public on the wisdom of dealing only with legitimate organizations.

"State enforcement and administrative offices," Mr. Selby said, "should be strengthened in order to make state enforcement measures more effective as opposed to a policy of surrendering authority and jurisdiction to federal authorities.

Praises Securities Business.

"Securities dealers and underwriters have contributed more to the upbuilding of American business and the American system of free enterprise than they have ever been given credit for doing. Now the industry as a whole is facing serious problems and, insofar as our supervision of their business can be made effective and of assistance to them, they should receive our support." Other officers elected for the ensuing year by the state commissioners are: Joseph Schneider, Kentucky, first vice president; Andrew J. Markey, Jr., New

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WALLACE H. FULTON

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Certain types of securities lend themselves to auction markets, he pointed out. However, he added: "The over the counter market is, after all, the backbone of the securities business, being a negotiation market. Actually, an exchange is only an adjunct to the investment business, taking care of transactions in those securities susceptible to auction trading."

Edward E. Chase, Maine Securities Company, appearing on behalf of the Maine Securities Dealers Association, also advocated more strict supervision over admission of securities to unlisted trading privileges.

Hearings on the proposed amendments to the securities act, ended last week. A subcommittee of the House Commerce Committee will now draft a proposed bill. This may take several months, it is believed.

Jersey, second vice president; Robert L. Smith, Jr., Minnesota, secretary, and Ethel McLees, South Carolina, treasurer.

In addition to Chairman Zeller, the NASC cooperative committee includes Walter C. Miller, Pennsylvania; Blake T. Newton, Virginia, Edwin M. Daugherty, California, and V. W. Huffman, Kansas.

Lowry Sweney of Columbus is chairman of the NASD committee engaged in this cooperative program.

Sweney on Cooperation

In his report to the recent Board meeting, Mr. Sweney said that "generally speaking" the average State regulatory Act can be roughly divided into the following classifications: registration and qualification; definition; exemptions; licensing and punitive sections. "I think it is the first subdivision (registration and qualification) that is ordinarily uppermost in the minds of those who talk about uniformity of state regulation," he stated. He referred to the multiplicity of forms, need-

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gram upon which such fine progress has been made.

"Problems and Difficulties"

"I am not unmindful of the problems and difficulties. NASD has been subjected to criticism in the past—some of which it did not deserve and some of which was based upon mis-information or a complete lack of pertinent facts. It is my hope that we will be able to spread knowledge about the Association and its program and objectives over the whole of the membership. In that way we can dispel misunderstanding that has been responsible for much of past criticism.

"As the representative on the Board from the Texas District for the last two years I have had an opportunity to participate in the development of the major activities undertaken by the Association and to know the forces underlying the decisions made by the Board. In every instance the action taken was dictated by considerations of the best interests of the business.

"I only want to say that the same considerations will guide us in the year that lies ahead."

Removal of Washington Office Under Consideration

Consideration is being given to removal of the main office of the Association from Washington, D. C. The Securities and Exchange Commission will move to Philadelphia in the near future. It is one of the agencies releasing present quarters to war-time organizations of the Government.

Transfer of the Washington office of the Association is being considered, first, because of the close contact that office has traditionally maintained with the SEC and its staff and, second, because of the question before all private organizations in Washington as to the necessity of their remaining in the Capital in view of the ever-growing requirements of the Government for existing office space.

The Board of Governors at its recent meeting informally reviewed these questions. Final decision was left to the judgment of the Executive Committee.

less duplication of returns and unnecessary variations existing in furnishing to many people different versions of essentially the same information.

He concluded his report by saying that Mr. Selby and Mr. Zeller have expressed a strong desire to walk further with NASD down the road of cooperation. "We on our part can do no less," he added.

Quotations Chairman Outlines Problems and Progress At Board Meeting

"Bugs" in Machinery Being Removed Weeden Declares, Reviewing Principles

Frank Weeden, Chairman of NASD's National Quotations Committee told the Board of Governors at its recent meeting that the new method of establishing published quotations was being successfully employed in the larger centers of the country. While pointing out that all of the "bugs" had not been worked out of the machinery, Mr. Weeden expressed the belief that District and Local quotations committees were striving to correct any inequalities. He was confident, he said, that in time the system would be working efficiently and without hardship on individual issues.

Mr. Weeden declared that under the new method recommended by the National Committee, each quoted security was to be considered separately in arriving at the proper spread, local committees deciding the size of the spread on the basis of "local market conditions with respect to such security, its activity, type, size of issue, price and other pertinent attributes." He recalled that in the National Committee's enunciation of principles for the guidance of local quotations committees, it was stated:

Describes Formula Base

"In computing the published bid price of a security, two or more of the best actual bids shall be taken into consideration. The bid price to be published shall not be less than the actual bids by more than the equivalent of a nominal selling commission. The published asked price shall be determined by adding to the price determined, pursuant to the above, the spread which has previously been assigned to the security by the Quotations Committee. This published asked price shall indicate a reasonable margin above the published bid price so as to afford retail dealers, exercising reasonable intelligence and skill in the purchase of such security, a fair and justifiable profit on the sale thereof."

Member May Petition

In conclusion, the point was stressed that a member may petition for a change in the spread assigned to a security upon evidence that he has a "substantial, definite and continuing interest in the security in question."

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When plans for the securities industry's participation were completed, NASD members were advised in two letters from Wallace H. Fulton, Executive Director, of the bases upon which this Association's membership could aid in the sale of Defense Bonds and Tax Notes. Simultaneously, the Investment Bankers Association, the Association of Stock Exchange Firms and the New York Stock Exchange acquainted their members with the details of the program.

Industry Issuing Agents

As a part of the industry's program, members of the Associations and of registered Stock Exchanges were accorded the privilege of becoming issuing agents of the Treasury in the distribution of Series E bonds as were the various Clearing House Corporations of stock exchanges. A number of members and financial center Clearing Houses had arranged to be such agents as this issue of the NEWS went to press. Due to the requirement that \$25,000 be posted to underwrite this privilege it was not expected that a great number of firms could become issuing agents but this need in no way interfere with their sale of Series E Bonds or the F and G series, it was pointed out. Arrangements could be made with local banks or Federal Reserve district banks to fill all orders.

With respect to the Tax Savings Notes, the securities industry was seen to have an unusually attractive opportunity to aid in the war effort. These Notes, members were told, were desirable for use of all taxpayers and the funds thus employed would in no sense affect available supplies of investment capital. All clients would be interested, it was felt, in having the advantages of these Notes brought to their attention.

Mr. Weeden said the principal problem in applying the new quotations formula was encountered in establishing spreads for inactive issues. In the main, he felt that active securities were not materially disturbed or their distribution hampered from the standpoint of the dealer. He said that local committees were endeavoring to weigh all factors involved when considering inactive issues and should, in a reasonable length of time, remove any existing unfair policies.

SEC Warns Against Abuses of Agency Relationship With Customer

Opinion Calls Attention To Fiduciary Obligation, Possibility of Fraud

A broker-dealer who acts as agent for both parties of a transaction may be perpetrating a fraud upon his customer, according to an opinion recently offered by James A. Treanor, Jr., Director, Trading and Exchange Division of the SEC in reply to questions based upon such an alleged practice.

The hypothetical example recited by Mr. Treanor follows: "An order is received from a customer to purchase for him a designated security at a designated price, for example 101½, or the customer may have definitely specified '101½ or better.' The broker-dealer telephones a second broker-dealer known to specialize in effecting transactions in this security and ascertains that he is willing to sell the security at 101¾. Instead of purchasing the security at this price on behalf of the customer, the first broker-dealer persuades the second one to employ him as agent to sell the security at 101½ and to pay him a commission of ½ point for effecting the transaction, which, after deduction of the ½ point commission will net the second broker 101¾, the price originally quoted by him. Thereupon, the first broker completes the transaction as agent for each of the parties and receives a commission from each."

Concerning this procedure, Mr. Treanor said: "In my opinion, such conduct on the part of the first broker constitutes an abuse of his obligation as a fiduciary which amounts to fraud upon his customer, and as such may constitute a violation of Section 17 (a) of the Securities Act of 1933 or Section 15 (c) (1) of the Securities Exchange Act of 1934 and Rule X-15C1-2 thereunder. In the Restatement of the Law of Agency by the American Law Institute, it is specifically stated: "The duty [of an agent] to obtain the terms most advantageous to the principal [who in the above case is the customer] exists even though the principal has fixed the price at which the agent is to buy or to sell. . . ."

Continuing his comment, Mr. Treanor says: "It makes no difference that the first broker-dealer may disclose to each party that he is acting as agent for both parties and the amount of commission to be received from each, as the abuse of fiduciary obligation consists in not obtaining the security for the customer by whom he was employed at the cheapest price possible."