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CHAIRMAN RITER ANNOUNCES PLANS FOR EXAMINATION OF MEMBERS IN 1943

By HENRY G. RITER, 3rd, Chairman

At the annual meeting of the Board of Governors in January, a program for uniform examination of all members in 1943 was adopted. The plan contemplates a much simplified, less expensive procedure this year under direct control of the Board.

The opinion was unanimous that 1943 should see no relaxation in our enforcement work. Another examination is to be made of all members and where conditions that are disclosed necessitate such action, the disciplinary procedure of the Association will be vigorously employed.

At its January meeting the Board agreed that the Association should this year concern itself primarily with the question of the sale of securities at prices which bear no reasonable relationship to prevailing markets. Our own experience of the past two years and several recent SEC decisions demonstrate that this question represents the most pressing problem.

In order to accomplish the objective of the Board in the most efficient way at our command and at a cost which can be borne, it was decided that members would be called upon to report the facts surrounding a fixed number of transactions which would be sufficient to reflect the pricing practices of the member. Forms to be filled out by the members will be mailed from the Executive Office and will be returned to that office for analysis. The form received by the member will carry a code number which will be the only identification on the schedule he fills out. One master file of code numbers will be kept in the Executive Office and while examiners in various Districts will be employed for analysis work, no examiner will be aware of the source of the information he is reviewing.

This strict confidential treatment of all material filed will be deviated from only when examinations disclose the possible necessity of further action by a District Business Conduct Committee.

It is the hope of the Board of Governors that the usual gratifying spirit of co-operation members have extended in the past will be accorded our program in 1943. The Board approved the method outlined only after careful study of its details. Many methods were considered before the one discussed was finally adopted.

One thing more. What you receive from the Association will not be a questionnaire made up of a lot of questions that sometimes appear to be listed simply to confuse or fill up space. The records you will need to fill out the form sent to you should be readily at hand. The time required to supply the facts needed will not be burdensome.

Looks to Public, Not Politics, as Future Aid for Securities Business

The National Association of Securities Dealers, Inc., affords the securities industry the means of safeguarding the future of that industry, Henry G. Riter, 3rd, NASD Chairman, said in an address February 4 at the annual dinner of the New York Security Dealers' Association. He warned against depending upon the "shifty winds of politics" for solution of the industry's difficulties, "real and imagined."

"Public attitude toward our business has undergone a great and salutary change," Mr. Riter said. "Recognition
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TREASURER REVIEWS DETAILS OF EXPENDITURES LAST YEAR

By ROBERT W. BAIRD, Treasurer, 1942

We spent a lot of money last year. The total was \$404,108 against an income of \$371,220. Because we had husbanded our funds pretty carefully in 1940 and 1941, the deficit was absorbed without difficulty.

Here is where most of the money went in the year ended

September 30 last (For details, see page 9):

1. District Committees, \$206,909.

The Association is divided into fourteen Districts. Each
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Finance Chairman Says 1943 Budget Down 30%

By WILLIAM A. FULLER,
Chairman, Finance Committee, 1942

The Association's budget for the fiscal year ending September 30, 1943, calls for a reduction of thirty per cent from expenditures of the last fiscal year. The budget for the current fiscal year provides for an expenditure of \$275,000.00 as compared with \$404,108.00 spent in the period ended September 30, 1942.

(The Treasurer, Robert W. Baird, in another column, discusses items which made up the total expenditure in the last fiscal year.)

On the basis of assessments collected to date and estimates of collections to be made in April, at mid-term, income of the Association this fiscal year should approximate \$250,000.00. Should revenues reach this projected figure, the Association will not cover all of its operating expenses on the basis of its current budget, but it is hoped that the latter will prove to have been generous. Last year was the first time since formation that the Association finished a year in the red, and this was the consequence of major undertakings which the Finance Committee realized from the start would be expensive.

Upon recommendations of a Special Assessment Committee made up of representatives of various classes of members, the Finance Committee in 1942 and prior to the opening of the present fiscal year approved a new assessment formula. It was subsequently adopted by the Board. As a result the former method of classifying members in several assessment categories was dropped in favor of a simpler system having three basic factors:

1. A \$30.00 annual assessment fee for all members;
2. Personnel assessment at the rate of \$3.00 and \$1.50 per head, depending upon the amount of time devoted to the member's securities business;
3. Assessment of underwritings at the rate of 1/100th of 1 per cent on all participations over \$100,000.00.

This formula made possible a minimum assessment of \$31.50 and provided a maximum of \$5,000.00 for any one member. Three members are paying the maximum this year. The formula permitted the Association to assess a larger number of underwriters than was possible under the previous schedule. In the current year, 280 members are paying assessments on underwritings, while in the preceding year, 169 paid on underwritings.

In addition, certain types of members with relatively large forces are paying a fairer proportionate share of the total assessment this year. That was the objective sought by the Special Assessment Committee—a more equitable allocation of the assessment among all of the members. True, some of the smallest members are paying larger assessments than heretofore, but the overall picture is one of more equitable distribution of the amount to be raised.

Members of the Finance Committee and of the Board were gratified by the reception given the assessment formula by the ranks of the membership. Few complaints were made and the fairness of the principle generally recognized.

Dewar Thanks Members for Co-operation

By H. E. DEWAR, Chairman, 1942

The year 1942 was one of the most difficult through which our business has ever passed, and it naturally follows that the period was one which produced an equal number of burdens for NASD.

In retrospect, one of the most gratifying features of the year's work was the whole-hearted co-operation given, almost without exception, by our members in the program of the Board of Governors. This is most heartening when you consider but a few of the major developments of the year.

There was, for instance, the membership-wide examination, unprecedented in its scope and nature. Regardless of the manner in which members in various parts of the country were reached or affected by this program, there was little or no inclination to impede the work of our staff people, or others representing the Association. Examiners were accorded fullest freedom and all that could be asked in the way of courteous consideration from those upon whom they called; questionnaires, more or less lengthy, were received in the mails in other places and even though they were sometimes difficult to understand and time-consuming to complete, members went ahead and complied with this obligation of membership seldom with any complaint; accountants hired by the Association called on the membership in all their actions and again these people were accorded every bit of co-operation essential to their work.

Members also will recall the problem presented to the Board by the release of a draft of a proposed new SEC rule identified as X-15C1-10—the "Disclosure of Market" rule. Over 900 letters were sent in to the Executive Office by the members on the subject of this rule. The Board's decision that the rule was unworkable and impracticable and the facts recited to the Commission in support of that conclusion were greatly aided by members' comments and suggestions on the draft sent to them.

There is still, of course, a small but rather vocal element that resents the burdens imposed by self regulation. Some of these even go to the extent of saying that they would prefer outside regulation. Such statements spring from a natural resentment which most successful businessmen have towards regulation of any sort.

Our business today is broader in its scope and personnel than it was when most of the honest critics of regulation started out. Securities are much more widely held and many holders have been added from the ranks of the financially unsophisticated. Such a process, while being a great force in preserving and strengthening our democratic institutions, brings added burdens and responsibilities to our financial community. In a recent article by Walter Lippmann, he cited the contrast between the old British and French aristocracies and how the latter lost out because they clung to their privileges without accepting responsibilities, while the British accepted heavy burdens, to live at least another day. Mr. Lippmann applied

(Continued on page 7, column 2)

EXECUTIVE DIRECTOR'S REPORT TO BOARD OF GOVERNORS, JANUARY, 1943

Following are extracts from the Annual Report of Wallace H. Fulton, Executive Director,
to the Board of Governors, January 18, 1943.

District Activities

As is my custom, I visited many of the Districts during the year, several times in the company of the Chairman, for conferences with District Committees. In the spring I met with Committee members in Los Angeles and San Francisco and in Denver. During the year visits were also had with District Committees in Boston, Minneapolis, Cleveland, St. Louis, Texas, Chicago, Washington, D. C., and Baltimore, as well as with Philadelphia and Pittsburgh members of District No. 12 Committee.

I also attended the annual convention of the National Association of Securities Commissioners at St. Paul, Minnesota, and delivered an address there. Chairman Dewar was a guest of the convention as were members of the Board and of the District Committee in that area. These conventions of the State Securities Commissioners afford an increasingly valuable opportunity for discussion of problems of concern to both our groups. The Association is indebted to the officers and members of the NASC for the cordiality and generous spirit of interest they have always displayed toward NASD representatives.

Membership

Membership in the Association declined steadily during the last year. As of December 31, we had 2,281 members representing a net decline during the year of 578 or 20 per cent.

(As of February 1, membership totalled 2,265.)

Ninety-four new members were admitted in 1942 while 666 memberships were terminated.

I believe you will be interested in an analysis of the membership decline. Due to the fact that resignations do not always disclose the exact cause for the action, our statistics are not perfect, but they are, nevertheless, reliable indicators. Of the 666 terminations, 358 occurred because of dissolution or retirement from the securities business. How many of these were the result of entry of the individual member or partners into the services we can only guess, but certainly a fair proportion reflected such a cause. As to the remaining 308, the letters of resignation of 75 stated that they were entering military service or war work and another 75 stated they were to be inactive for the duration; 22 of the total resignations resulted from mergers; 42 from expulsion either by NASD or the SEC; 65 were cancelled out for non-payment of assessments and the balance were for miscellaneous causes such as death, illness or other personal reasons. In retrospect then, it would appear that at least 25 per cent of the membership loss of the past year was directly traceable to entry of the principals into war services; another 25 per cent was for causes such as death, illness, expulsion or failure to meet member-

ship obligations and 50 per cent for all other business causes, including the impact of the war upon personnel, volume of business and so forth.

The largest proportionate decline in membership during the last year occurred in District No. 11—the Baltimore-Washington, D. C., area. Due in part to the number of expulsions in that District, the decline in membership in 1942 amounted to 35 per cent against the 20 per cent decline for the Association as a whole. In the New York District the decline was approximately 22 per cent; Chicago and California, 20 per cent; Boston, 18 per cent; Ohio, 10 per cent; the South and Pennsylvania, 15 per cent each.

Our membership statistics are much more sensitive to trends and spontaneous developments than are the registration statistics of the SEC and for that reason I hesitate to make any direct comparison between our separate experiences. However, for purposes of simple comparison: As of December 31, 1941, SEC registrants numbered approximately 5,840 and at the end of 1942 approximately 5,075, a decline of 765 or just over 13 per cent of their total. At the end of 1942, 45 per cent of SEC registrants were members of NASD, at the end of 1941, 49 per cent.

Enforcement

In the past I have always included in my report to the Board a discussion of various aspects of the Association's examination and enforcement work between Board meetings. At this time I wish to make a more extended report on Association business conduct activities than has heretofore been customary. This report will cover much of the development and evolution of the Association's examination and enforcement program since the Board meeting in Washington in April, 1941.

Our examination program developed in different ways. The first concerted examinations were mass examinations of all members, first in District No. 4 (Minnesota) and then in District No. 3 (Colorado). It was found that this type of examination method was most effective for Association purposes. However, it was also quickly ascertained that problems of disposition of the force of Association examiners would make difficult a continuation of this system.

District No. 14 (Maine, Massachusetts, New Hampshire, Rhode Island and Vermont) commenced its examination program with a slightly different approach. The Committee hired Certified Public Accountants to conduct examinations of all members, with particular emphasis to be placed upon the financial condition and profit policies of the members.

District No. 8 (Illinois, Indiana, Iowa, Michigan, Nebraska and Wisconsin) was the first District to experiment with a questionnaire. In the early fall of 1941

that Business Conduct Committee conducted a questionnaire and follow-up examination of 27 member firms in and around Indianapolis.

This first experiment by the Association with questionnaires demonstrated that this method could be used effectively to point out those firms which should be given further and more thorough examination and could be used effectively to ascertain those matters which the Board has determined in April 1941 to be paramount. It also appeared to be a less expensive method than the personal examination.

Various forms of questionnaires were devised by the District Business Conduct Committees in order to complete examination of all the members of the Association during 1942. Altogether, 10 Districts employed the questionnaire method to complete their examinations. Those questionnaires were of different types and employed different approaches to the problem taken by the various Committees. For instance, several of the Districts did not include any request for information on profit policies. Other Districts included requests for a statement of the profit policy of the firm, in general terms, while the majority required the member firms to submit 25 or 50 consecutive principal transactions with customers. It was found, through this latter method, that those firms whose profit policies might be considered questionable could be separated from the rest, and thus Association attention could be more readily focused upon these possible violators of the Rules of Fair Practice concerned.

In addition to all the foregoing, personal examinations were conducted by the Secretaries and accountant examiners in various Districts, where, upon information and belief, the District Business Conduct Committee felt that an examination was warranted.

Last spring the Board decided, on the basis of experience to that time, that future examinations should be conducted on a national scale by the questionnaire method, with follow-up examinations where necessary and to be supervised by the executive office under the direction of the Board of Governors. This was determined to be desirable from the point of view of cost, and, in addition, to develop a greater uniformity of examination method throughout the country.

The result of experience has been that the questionnaire method can be adopted for future use, with the reasonable belief that it will point out those matters with which the Association is most concerned and those firms which should have further and continued examination.

The type of questionnaire to be used will be different from any used last year. Greater emphasis will be placed on profit policies, and a check will be made in every instance to ascertain if securities are sold at prices reasonably related to the markets. Particularly is this true now that the Commission, through promulgation of Rules X-17A-5 and X-15C3-1, has assumed more direct supervision of the finances of all registered brokers and dealers.

In one District last year a Business Conduct Committee filed a complaint against a member because that member knowingly submitted false information in answer to a questionnaire to the Committee regarding its financial condition. When this situation was discovered, the Committee was furnished additional information by the member in

question, which also turned out to be false. The Business Conduct Committee took the position that the firm was on the verge of insolvency and at the same time had knowingly submitted false information to it. The Committee expelled the firm. The firm appealed, admitted the truth of the charges but contended that the penalty was excessive. The Board affirmed the expulsion order by the District Business Conduct Committee upon the recommendation of the National Business Conduct Committee. It seems to me that a decision of this nature has many important implications and is a precedent for future enforcement work, particularly now that future examination work is to be conducted largely by means of the questionnaire method.

Another District Business Conduct Committee has recently taken action in a case involving a practice of selling securities at unfair prices. The member concerned had previously been warned informally by the Committee that its profits in principal transactions were not in line with the best practices of the business, and, in addition, that the firm was selling securities at prices not reasonably related to the market. Upon a follow-up examination this past summer, it was found that there was still substantial cause for criticism on the same grounds. The firm in question had developed a theory of average profit per transaction based on the amount of money involved and the cost of the security. The question of services to the customer and expense of operation appeared to be secondary. In round figures, the firm had a practice of charging as near to 10 per cent mark-up on trades as possible. At the hearing before this Business Conduct Committee, the firm stated that it had further revised its policies subsequent to the examination and prior to the filing of the complaint. However, despite this, the Committee felt that a sharp warning would not be effective, inasmuch as this was the second cause for criticism of the firm, and it thus determined upon a fine of \$1,000.

In addition, the Business Conduct Committees have taken disciplinary action in such cases as manipulation, renegeing on contracts, violation of the pegging, fixing and stabilizing rules, and quite a few instances of insolvency. Thus, it will be seen that the Business Conduct Committees have been presented with many and varied problems. However, I believe that the question of profit policies has been and is the predominant problem in all Districts.

(See tabulation on page 5 for statistics on complaints.)

Disclosure Rule—X-15C1-10

It will be recalled by members of the Executive Committee and other members of the Board that I informed them in June that the Commission was preparing to propose a new rule which would require disclosure of bid and asked prices to customers on transactions in over-the-counter securities. I reported that when drafted the proposed rule would, as had always been the custom, be circulated confidentially among interested organizations and groups representative of those who would be affected by such a rule. Several weeks later the proposed rule, labeled "Disclosure of Market Price," and designated "X-15C1-10" was released by the Trading and Exchange Division but instead of this proposal being circulated in its original draft

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National Business Conduct Committee Reports Disciplinary Experience

By **LAWRENCE B. WOODARD, Chairman,**
National Business Conduct Committee, 1942

The National Business Conduct Committee, made up of members of the Board of Governors, serves the Association as a review and appeals board of all disciplinary decisions of District Business Conduct Committees. It considered ninety-nine cases decided by District Business Conduct Committees last year. Twenty-five of these cases were formally presented to the Committee either on appeal by the member involved or on review instituted by the Committee itself; and in these twenty-five cases the Committee handed down decisions upholding the original decisions of District Committees, or the Committee amended, remanded, or reversed them. It was found necessary to modify four decisions, and to reverse District Committees in four other decisions.

We have noted several things in our work of the past year, particularly that the great percentage of the problems presented to the National Business Conduct Committee concern the matter of sales of securities at unfair prices

or at prices not reasonably related to the current market of the securities in question.

It is my belief that the National Business Conduct Committee should act as a stabilizer among the District Business Conduct Committees and that, insofar as possible, it should endeavor to develop a uniformity of business conduct policy as distinguished from decisions. We appreciate that many varying circumstances enter into and affect the particular decision in each case, as, for instance, the amount of fine or extent of penalty, and I believe the National Business Conduct Committee feels as a whole that the decision of a District Business Conduct Committee should not be altered or set aside unless substantial reason is shown for doing so.

The National Committee, after all, is an appellate body and is not in the position of a Committee of the first instance. However, responsibility on behalf of the Board is one which it cannot neglect.

It is neither a pleasant nor an easy task with which the National Business Conduct Committee is charged. However, I believe that any Committee so situated should exert its authority in the interests of the Association and in observance of national policies of this Association as enunciated by the Board of Governors.

COMPLAINTS AND DECISIONS—1941

Dist. No.	Complaints Pending Jan. 1, 1941	Complaints Filed During 1941	Complaints Referred by SEC	Complaints Closed During 1941	Complaints Pending Dec. 31, 1941	Fines	Expulsions	Suspensions	Censures	Appeals for Review	Reviews Instituted by NASD
1	..	6	..	4	2	1	3	1	..	..	..
2	1	11	3	11	1	7	1	..	7	..	..
3	..	5	..	1	4	1	..	..	1	..	..
4	..	10	1	10	..	8	1	..	9	1	..
5	..	..	..	..	..	..	..	..	..	..	..
6	1	..	..	1	..	..	..	1	..	..	..
7	..	..	..	..	..	..	..	..	..	..	..
8	..	23	2	6	17	4	1	..	1	..	1
9	..	..	..	..	..	..	..	..	..	..	..
10	..	3	..	3	..	2	..	..	2	..	..
11	..	9	..	7	2	..	6	..	1	1	..
12	..	7	1	1	6	..	..	..	1	..	..
13	1	33	11	22	12	..	13	3	3	2	1
14	..	13	2	9	4	6	1	1	5	3	1
TOTAL	3	120	20	75	48	29	26	6	32	7	3

COMPLAINTS AND DECISIONS—1942

Dist. No.	Complaints Pending Jan. 1, 1942	Complaints Filed During 1942	Complaints Referred by SEC	Complaints Closed During 1942	Complaints Pending Dec. 31, 1942	Fines	Expulsions	Suspensions	Censures	Appeals for Review	Reviews Instituted by NASD
1	2	2	..	4	..	2	1	..	..	..	..
2	1	5	1	6	..	4	..	1	3	1	1
3	4	1	..	5	..	2	..	..	1	..	..
4	..	..	..	..	..	..	..	..	..	..	..
5	..	1	..	1	..	1	..	..	1	..	..
6	..	..	..	..	..	..	..	..	..	..	..
7	..	1	..	1	..	..	1	..	..	..	..
8	17	7	2	21	3	2	7	4	2	2	4
9	..	1	1	..	1	..	..	..	..	..	..
10	..	3	..	3	..	2	..	..	1	1	..
11	2	4	..	6	..	..	5	..	..	2	..
12	6	5	..	11	..	10	..	..	..	..	..
13	12	23	8	33	2	13	10	4	4	4	3
14	4	4	..	7	1	..	5	..	1	1	..
TOTAL	48	57	12	98	7	36	29	9	13	11	8

OFFICERS for 1943

Chairman

HENRY G. RITER, 3RD Riter & Co.—New York

Vice-Chairmen

LAWRENCE B. WOODARD—Woodard-Elwood & Co
Minneapolis

E. WARREN WILLARD—Boettcher and Company
Denver

Treasurer

JAMES PARKER NOLAN—Folger, Nolan & Co., Inc.
Washington, D. C.

Executive Director

WALLACE H. FULTON—Philadelphia, Pa.

Executive Committee

Henry G. Riter, 3rd
Lawrence B. Woodard
E. Warren Willard
Ralph Chapman
Hermann F. Clarke
Lee M. Limbert
James Parker Nolan
Wallace H. Fulton,
Ex-Officio

Finance Committee

F. Edward Bosson, Chairman
Henry G. Riter, 3rd James Parker Nolan
Beardslee B. Merrill
Wallace H. Fulton, Ex-Officio

BOARD OF GOVERNORS

NAME	TERM EXPIRES (JANUARY)	MEMBER	CITY
DISTRICT NO. 1—(Idaho, Oregon, Washington)			
BEARDSLEE B. MERRILL	(1944)	Richards & Blum, Inc.	Spokane
DISTRICT NO. 2—(California, Nevada)			
MARK C. ELWORTHY	(1945)	Elworthy & Co.	San Francisco
RALPH E. PHILLIPS	(1946)	Dean Witter & Co.	Los Angeles
DISTRICT NO. 3—(Arizona, Colorado, New Mexico, Utah, Wyoming)			
E. WARREN WILLARD	(1945)	Boettcher and Company	Denver
DISTRICT NO. 4—(Minnesota, Montana, North Dakota, South Dakota)			
LAWRENCE B. WOODARD	(1944)	Woodard-Elwood & Co.	Minneapolis
DISTRICT NO. 5—(Kansas, Oklahoma, West Missouri)			
JOHN H. BARRET	(1946)	Stern Brothers & Co.	Kansas City
DISTRICT NO. 6—(Texas)			
WM. P. SMALLWOOD	(1946)	Smallwood & Company	Fort Worth
DISTRICT NO. 7—(Arkansas, East Missouri, West Kentucky)			
ALBERT THEIS, JR.	(1945)	Albert Theis & Sons, Inc.	St. Louis
DISTRICT NO. 8—(Illinois, Indiana, Iowa, Michigan, Nebraska, Wisconsin)			
RALPH CHAPMAN	(1946)	Farwell, Chapman & Co.	Chicago
R. WINFIELD ELLIS	(1946)	Lee Higginson Corporation	Chicago
W. S. GILBREATH, JR.	(1944)	First of Michigan Corporation	Detroit
DISTRICT NO. 9—(Alabama, Florida, Georgia, Louisiana, Mississippi, South Carolina, Tennessee)			
HAGOOD CLARKE	(1945)	Johnson, Lane, Space and Co., Inc.	Atlanta
DISTRICT NO. 10—(Ohio, East Kentucky)			
EDWARD BROCKHAUS	(1944)	Edward Brockhaus & Co.	Cincinnati
DISTRICT NO. 11—(District of Columbia, Maryland, North Carolina, Virginia, West Virginia)			
JAMES PARKER NOLAN	(1946)	Folger, Nolan & Co., Inc.	Washington, D. C.
DISTRICT NO. 12—(Pennsylvania, Delaware)			
SAMUEL K. CUNNINGHAM	(1945)	S. K. Cunningham & Co., Inc.	Pittsburgh
DISTRICT NO. 13—(Connecticut, New Jersey, New York)			
F. EDWARD BOSSON	(1944)	Putnam & Co.	Hartford
JAMES COGGESHALL, JR.	(1945)	The First Boston Corporation	New York
LEE M. LIMBERT	(1944)	Blyth & Co., Inc.	New York
HENRY G. RITER, 3RD	(1946)	Riter & Co.	New York
CLARENCE E. UNTERBERG	(1945)	C. E. Unterberg & Company	New York
DISTRICT NO. 14—(Maine, Massachusetts, New Hampshire, Rhode Island, Vermont)			
HERMANN F. CLARKE	(1944)	Estabrook & Co.	Boston

Executive Director's Report to Board of Governors, January, 1943

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form only among a limited group directly representative of affected parties, it was sent to a much larger group and thus got into the hands of the press.

After conferring with the Executive Committee on this development, a copy of the proposed rule was sent to members with the request that upon study of the proposal, comments and suggestions thereon be sent to the executive office. In all, some nine hundred letters were received. Of this number, exactly six voiced unqualified approval of the proposal and each of these members was largely engaged in stock exchange activities. The consensus was that the rule was wholly destructive, would not accomplish the objective evidently intended, and certainly that if it were adopted, there would be no further need for the Association.

An Executive Committee meeting was held in Chicago on August 11 to discuss the course of action to be taken by the Association on this proposal in the light of members' comments and suggestions. A meeting of the Executive Committee of the Investment Bankers Association was simultaneously being held in Chicago and at the request of John Fleek, our Executive Committee met with the IBA Committee for an informal discussion of the rule. The Executive Committee informed the IBA group that it had formulated its plan of procedure with respect to the proposal and that this plan would be pursued without regard for action to be taken by any other group in the industry except that the Association would be glad to keep such groups, representative of the membership, informed of its intended course of action as this evolved.

A week later the Executive Committee met with the Commission in Philadelphia. The Committee spoke freely and frankly to the Commission about the proposed rule and our position in respect to it. Following this meeting, at the direction of the Executive Committee, the executive office began drafting a memorandum to be submitted to the Commission on the proposal. In keeping with the understanding had in Chicago, the Executive Committee informed the IBA and, also, the Association of Stock Exchange Firms and other organized groups of the industry, when the memorandum had been drafted in tentative form. The Executive Committee told these groups it would be glad to discuss the memorandum with them. A meeting was held for the purpose in New York on October 8.

The memorandum was read to the meeting by Chairman Dewar and each of those present was asked in turn to offer comments and criticism. As a result a representative of every segment of the securities business was given an opportunity to consult with the Executive Committee on the final product. No alternative proposal was suggested. A meeting of the Executive Committee was held in New York on October 20 to consider the final draft of the memorandum and the covering letter to the Commission. The memorandum and accompanying letter were unanimously approved by the Executive Committee and on October 22 they were delivered in person by the Executive Director to each Commissioner and to the Director of the Trading and Exchange Division, Mr. James A. Treanor, Jr.

SEC Relations

Any fair-minded review of the situation will disclose that opportunities exist on both sides for strengthening and for making our relations with the Securities and Exchange Commission more productive of mutually satisfactory ends. The incentive is fundamental—the Commission and ourselves are concerned with phases of the same problem.

Concerned with the same problem in different forms, the Association and the Commission have a natural community of interest. Differences have and perhaps always will arise as to precise methods best suited to the solution of various types of problems but the ultimate objective cannot be lost sight of, and that should be the most vital concern of both.

That the Commission is favorably inclined toward united endeavors to solve problems common to the business was evidenced several months ago when Chairman Purcell invited representatives of various organizations and groups to meet with the Commission to discuss some of these matters. The following men attended several meetings with the Commission and staff and formed sub-committees from among the securities business to continue conferences on specific subjects: for the National Association of Securities Dealers, Inc., H. H. Dewar and Wallace H. Fulton; Investment Bankers Association of America, John S. Fleek; New York Stock Exchange, Emil Schram; Association of Stock Exchange Firms, James F. Burns, Jr.; Philadelphia Stock Exchange, Edgar Scott; Pittsburgh Stock Exchange, the late Marshall R. Barbour; New York Curb Exchange, Fred C. Moffatt; Detroit Stock Exchange, Andrew Reid. The sub-committees were assigned the following topics for study and report to the ranking Committee of the business and the Commission: "War Problems"; "Operating Expenses"; "Uniform Reporting"; "Corporate Accounting Practice"; "Exchange Trading Practices"; "Co-operation Between Exchanges"; "Public Utility Problems."

Some progress has been made by certain of these groups in attacking and solving their specific problems. Noteworthy in this regard were the efforts of the Committee on the uniform financial report.

Dewar Thanks Members for Co-operation

(Continued from page 2)

this to U. S. business and said we would suffer the fate of the French nobility unless we stopped brooding upon our troubles and diminishing immunities, and took constructive advantage of our opportunities in a changing world. I think this applies with great force to the investment business.

Those of us who have been close to the processes of self-regulation feel that it gives us a constructive opportunity to improve the standards—not of those who have conducted their affairs properly—but of the investment industry as a whole. By so doing, the lot of all of us will be improved through the increased prestige of the business and its more universal ability to render real service to economic society. These results can best and most quickly be achieved if the NASD can have the benefit of a constructive attitude from all of its membership.

Treasurer Reviews Details of Expenditures Last Year (Continued from page 1)

has a District Committee selected by the members of the District. There are, in most instances, several subsidiary committees. Each has an important job. Most important of them all is the Business Conduct Committee's. The biggest share of the money spent by the Association is on business conduct work. We began an aggressive program of enforcement of Association Rules in mid-1941. Everyone on the Board knew it was going to cost a lot of money. Some of it was spent mistakenly, we realized after we got going. The same mistakes aren't being made now and the continuing program is going to cost a lot less than it did the first year or so. All in all, the fourteen Business Conduct Committees in the last fiscal year spent about \$75,000.00 to carry on their work, aside from salaries of paid personnel. (None of our committee people receive any compensation.) The fourteen District offices paid salaries amounting to \$96,000. Thirty-nine employees were paid that amount. The balance, about \$31,000, was spent for rent, postage, quotations, printing and stationery, and the usual miscellaneous things.

2. National Office, \$91,794.

Salaries of seventeen people employed in the executive office account for \$58,120 of the total. The other principal items of expense were printing and stationery (\$12,700); rent (\$8,000). As the Chairman for one year and Treasurer for another, both of which jobs permitted of close attention to the personnel and work of the executive office, there is no doubt in my mind of the need or ability of the employees there or that the Association gets full value per dollar spent.

3. Traveling and Meeting Expense, \$40,733.

This represents amounts of reimbursements to members of the Board of Governors, Executive Committee, Finance

Committee and other national committees for out-of-pocket cost to them of attending several meetings during the year and it also includes the cost of the meetings themselves. In a desire to economize, fewer meetings of all committees and of the Board were held last year than in previous years. We saved probably several thousand

dollars, but it isn't certain that this economy was in the best interests of the Association and its members. It costs money to draw men from all over the country to one location for a meeting which may last from one to three days. But this is serious business and important to our business. It's hard to evaluate it in dollars and cents, and probably you can't.

4. General Expense, \$64,672.

Mostly counsel fees and expenses. Our counsel is on a modest annual retainer and practically all of last year's fees were for special work—the Public Service of Indiana disciplinary cases which are up for review before the SEC and which have cost a considerable amount. Another item of counsel cost last year was the Association's intervention in several requests of the New York Curb to extend unlisted trading privileges to securities enjoying over-the-counter markets. We hope to win in some of the cases. Members and the Board favor continued study by the Association of all such applications of the Curb or other exchanges in the interests of the over-the-counter markets.

That in summary form is where the money went. It's somewhat in the nature of history because figures for the final quarter of the fiscal year (the three months ended September 30, 1942) showed a substantial reduction in expenditures and those for the

three months ended December 31, 1942, a further reduction. We hit a peak in expenditures in the middle of the last fiscal year and the trend has been downward since.

National Association of Securities Dealers, Inc.

BALANCE SHEET

As at September 30, 1942

ASSETS

Cash in bank and on hand:		
The First National Bank, Philadelphia, Pa.:		
Treasurer's account	\$175,228.36	
Working fund account	5,502.80	
Petty cash fund, Philadelphia, Pa.	50.00	
Petty cash fund, New York, N. Y.	500.00	
		\$181,281.16
Receivables, per contra:		
Assessments	\$255.00	
Subscriptions to Manual	15.00	
		270.00
Deposit with American Airlines, Inc.	425.00	
Deposit with Post Office	100.00	
Advances for traveling expenses	500.00	
Office equipment and furniture		
(Charged to expense when purchased)		
		\$182,576.16

LIABILITIES

Accounts payable	\$24,487.25	
Deferred credits:		
Receivables uncollected, per contra	\$270.00	
Fines and costs collected, pending review	28,855.80	
		29,125.80
Surplus:		
Balance—September 30, 1941	\$161,851.16	
Deduct: Excess of expense over income for the period from October 1, 1941, to September 30, 1942	32,888.05	
		128,963.11
		\$182,576.16

STATEMENT of INCOME and EXPENDITURES

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

INCOME:	Fiscal Year Ended September 30	
	1942	1941
Assessments Collected	\$368,024.75	\$342,258.00
<small>Being dues paid by 2,883 members in year ended September 30, 1942.</small>		
Branch Office Registration Fees	2,930.00	3,010.00
Other	285.00	240.00
TOTAL INCOME	\$371,219.75	\$345,506.00
 EXPENDITURES:		
<i>National Office:</i>		
Salaries	\$58,120.21	
<small>Paid to 17 employees, including Executive Director, Assistant, Comptroller, Examiners, Stenographers, Clerks, Accountant.</small>		
Legal Fees and Expenses	57,941.39	
<small>Largely "special fees" resulting from Public Service of Indiana review by SEC; opposition to N. Y. Curb Exchange applications for unlimited trading privileges and miscellaneous special services of counsel, as well as annual retainer.</small>		
Travel and Meeting Expense of Board of Governors, Advisory Council	18,253.64	
<small>There are 21 members of the Board and 14 members of Advisory Council.</small>		
Travel and Meeting Expense of National Standing and Special Committees	13,437.85	
<small>There are five standing committees and in 1942 four special committees served.</small>		
<small>NOTE: Above two items represent actual out-of-pocket expense incurred by members of Board and Committees and cost of meetings attended by such members, all of whom serve without compensation.</small>		
Employee and Miscellaneous Travel and Meeting Expense	11,041.22	
<small>Includes expense of national meeting of District Secretaries and Chairmen, also travel expenses of members of committees from Board of Governors.</small>		
Printing and Stationery	12,733.99	
Office Rent	8,128.17	
All Other Expenses	19,542.38	
<small>Includes insurance and taxes of \$5,181 and miscellaneous charges, no one of which exceeded \$5,000.</small>		
Total Expense National Office	\$197,198.83	\$190,830.81
<i>District Committees' Expense:</i>		
<small>NOTE: Following items of expense cover fourteen District Committees.</small>		
Salaries	\$96,290.06	
<small>Paid to twelve District Secretaries, eight Examiners and four temporary Examiners, nineteen Stenographers, Clerks, etc.</small>		
Examinations and Complaints	58,147.04	
<small>Cost to Association of enforcement work, excluding salaries of regular employees but including District Committees' legal fees and expenses, Public Accountants' fees and expenses, etc.</small>		
Travel and Meeting Expense	11,890.09	
<small>Being actual out-of-pocket cost to members of various committees incurred in attending meetings, etc., and cost of such meetings. All committee members serve without compensation.</small>		
Rent	10,791.01	
All Other Expense	29,800.77	
Total Expense of District Committees	206,908.97	128,128.72
TOTAL EXPENDITURES	\$404,107.80	\$318,959.53
Excess of Expenditures Over Income	\$32,888.05	
Excess of Income Over Expenditures		\$28,546.47

NOTE: Members will be interested in reading accompanying statements by the Treasurer and Chairman of the Finance Committee.

Financial Report Requirements of SEC; Rule X-17A-5

The filing of annual reports of financial condition pursuant to Rule X-17A-5 of the Securities and Exchange Commission is now required of every member of a national securities exchange who does business with the public, every broker and dealer who transacts a business in securities through the medium of a member of a national securities exchange, and every broker and dealer registered as such with the Commission.

The provisions of the rule have confused a number of brokers and dealers. In general, the rule provides:

1. All brokers and dealers to whom the rule applies must file the report of financial condition during each calendar year, provided the report so filed is as of a date not more than 45 days prior to the filing thereof and that reports for any two consecutive years be not filed within less than 4 months of each other;

2. Those brokers and dealers who, during the year preceding the date as of which their financial condition is reported, have not made a practice of (a) extending credit in any form to customers (such as carrying margin accounts or selling securities on a partial payment or installment basis); (b) holding securities owned by customers, except as an incident to transactions with or for customers which are promptly consummated by delivery; or (c) carrying credit balances for customers except as an incident to transactions with or for customers which are promptly consummated by payment *are not required* to file reports certified by independent certified public accountants or public accountants, PROVIDED, such brokers and dealers are not required to file audited reports with any state in which they do business or with any national securities exchange of which they are members.

Thus, only those brokers and dealers who have made a practice of engaging in the type of business referred to above or who are required by state law or regulation of a national securities exchange of which they are members, are required to file certified reports of financial condition with the Commission.

3. The reports of financial condition are to be filed in duplicate at the regional office of the Commission for the region in which the broker or dealer has his principal place of business.

In issuing Rule X-17A-5, the Securities and Exchange Commission also released instructions and Form X-17A-5 as a guide for compliance with the Rule. Both the text of the Rule and this form should be read by registrants as a safeguard against unwitting violation of the Rule.

Since its original issuance, the Rule has been amended in one important respect. Certain schedules ("A," "B," "C") and valuations which are required to be filed as supplementary information will be treated confidentially and excluded from public inspection *when they are bound separately* from the remainder of the report.

(Continued from page 1, column 2)

of it as a vital and essential element of the national economy is widespread and expanding every day. I, for one, would rather trust the public and its capacity to assess our business in the light of fair and honest service rendered at reasonable cost to the investor than to trust the future of our business to the shifty winds of politics.

"We in the securities business must look upon our self-regulating activities as an investment in the continuing health of that business and as insurance of its future. The code of ethics which guides our efforts is not a static thing. Even before your Association or the Investment Bankers Association developed and enunciated ethical principles for respective members and even before they were drafted by the investment bankers code committee under the NRA, the ethical standards of our business were well established and recognized. The code formalized them, NASD adopted them as its creed, and they are now a guide of record. But this is not the end, merely the beginning. We are constantly improving both the letter and the spirit of the standards of commercial honor and just and equitable principles of trade in our business. It now seems within our grasp to place those standards on a high professional plane. It would be a serious mistake for us to entrust that opportunity to someone else. In my judgment, it should be our purpose to pre-empt for ourselves as much regulatory power as it is within our capacity to handle.

"We are daily being reminded of a new and immense responsibility that is developing as a part of the war program—developing just as rapidly and with just as much force as the production of the implements of war. I refer to the new army of investors which the government's financing program has probed. Its ranks are being expanded every day, in some part because of the unselfish contributions that are being made by the securities business. Our satisfaction with the importance of those contributions to the successful prosecution of the war is soundly justified but let us not neglect to recognize that this same army of investors will present a different kind of responsibility in the years that lie ahead than we have been discharging in winning thousands to its ranks. Many thousands of people who never before owned a bond or a share of stock are now capitalists in the truest sense of the word. The securities industry should be the first to concern itself with ways and means of safeguarding this national resource of capital. It may be axiomatic that 'the fool and his money are soon parted' and that no law can ever erase that truth. On the other hand, the securities business, in its own self-interest, should see to it that if and when public losses are sustained again that that business will not serve as the scapegoat.

"The NASD affords us the means of accomplishing that end. It should not be a negative force. I believe it would be dangerous for our business to be persuaded that it could relax and let the trend of events solve our problems for us. Some of our friends have interpreted the November elections as a sign that enterprise, and particularly the securities business, is to be relieved of regulatory restrictions imposed by government in the last decade. They would have us believe that the political trend is a promise of a cure for all of our difficulties, real and imagined. Let us not be beguiled by such ill-conceived reasoning."