



SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

DIVISION OF
MARKET REGULATION

June 18, 1982

Mr. Gordon S. Macklin
President
National Association of Securities Dealers, Inc.
1735 K Street, N.W.
Washington, D.C. 20006

Dear Mr. Macklin:

The Division has become concerned over apparent misunderstandings within the broker-dealer community about the status under the Securities Exchange Act of 1934 ("Act") of securities salespersons designated as independent contractors. Questions have been raised as to whether these persons are subject to the Act, whether they come within the definition of associated persons in Section 3(a)(18) of the Act, and whether they are employees subject to coverage by a broker-dealer firm's fidelity bond. These issues have surfaced recently because of the increasing number of firms denoting their salespersons as independent contractors. The Division is concerned that some securities salespersons calling themselves independent contractors have failed either to register with the Commission as broker-dealers or with a self-regulatory organization ("SRO") as associated persons of a registered broker-dealer. In order to forestall any regulatory problems relating to such developments, I would like to take this opportunity to restate the Commission's long-standing policy toward independent contractors.

The Act requires that a person selling securities be registered with the Commission as a broker-dealer under Section 15(a) unless he is an associated person as defined in Section 3(a)(18) of the Act. These two categories encompass the universe of persons engaged in the purchase or sale of securities. The term independent contractor does not appear either in the Act's definition of associated person in Section 3(a)(18) or elsewhere; thus, merely denoting a salesperson as an independent contractor does nothing to resolve the status under the Act of a given individual. The critical question is whether a so-called independent contractor's activities are subject to control by a broker-dealer within the scope of Section 3(a)(18) of the Act. Without that control relationship, the salesperson must be registered individually as a broker-dealer.

Confusion concerning the issue of "control" seems to be at the core of the independent contractor debate. The presumption that an independent contractor, by definition, cannot be subject to the control of an employer broker-dealer is incorrect. Pertinent

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agency law makes it clear that an individual can be denoted properly as an independent contractor and still be subject to the control of an employer if their relationship is one of principal and agent or master and servant. Distinguishing between the independent contractor who acts as a principal rather than as a servant or agent is a question of fact. Each situation must be scrutinized to determine how much control can be exercised by a broker-dealer over the acts of the independent contractor.

It has been a long-standing policy of the Commission that independent contractors whose selling activities were controlled by their broker-dealer employers could be characterized as employees for the purposes of the Act. As early as 1945, ^{1/} prior to the introduction of the term "associated person" in the Act, the Commission identified "control" by a broker-dealer as the sole standard for determining whether a person was an employee for purposes of attaching liability to a broker-dealer employer under Section 15(b) of the Act. ^{2/} At that same time, the Commission stated that use of the term "employee" in Commission rules or releases could include free-lance salesmen or other persons whether or not such persons would be deemed employees in some statutory context other than the federal securities laws.

Neither of these Commission interpretive positions was changed with the introduction of the concept of "associated person" to the Act by the Securities Acts Amendments of 1964. Indeed, the legislative history of Section 3(a)(18) of the Act makes it clear that the phrase "associated person" was created "for convenience of reference" to newly adopted statutory provisions of the Act which authorized direct disciplinary action against individuals. ^{3/} There was no desire to alter the Act's applicability to persons previously held to be employees, i.e., salespersons controlled by a firm, including those who were independent contractors. Rather, the Commission's General Counsel, now Commissioner Loomis, stated that the purpose of the new definition was to preserve the Act's existing applicability to persons controlled by a broker-dealer

^{1/} Securities Exchange Act Release No. 3674 (April 9, 1945).

^{2/} Section 15(b) of the Act authorized the Commission to deny or revoke the registration of any broker-dealer if it found (1) that such action was in the public interest and (2) that such broker-dealer, or any partner, officer, director or branch manager, or any person controlling or controlled by such broker or dealer, had been convicted within ten years or was enjoined in connection with activity involving securities, or had willfully violated any provision of the Securities Act of 1933 or the Act or any rule thereunder.

^{3/} S. Rep. No. 379, 88th Cong., 1st Sess. 1642 (1963)

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or controlling a broker-dealer, such as partners, officers and directors. 4/ Section 3(a)(18) was drafted to incorporate almost identical language to that already appearing in Section 15(b) of the Act. Thus, it is clear that the independent contractor salesperson may be deemed to be an employee and associated person under the Act if the requisite control relationship exists.

Accordingly, independent contractor salespersons who act as independent principals, in selling or inducing the purchase or sale of securities must be registered with the Commission as broker-dealers. Likewise, an independent contractor salesperson, whose activities are subject to control by a broker-dealer, whether by contract or otherwise, must be registered with a SRO as an associated person and should be covered by the employer broker-dealer's fidelity bond. Broker-dealers may not shift their obligation to control or supervise the activities of their independent contractor salespersons who are associated persons, and contractual terms that attempt to limit broker-dealer liability for the acts of such persons under the federal securities laws are of no effect.

While we believe the SROs have consistently required their members to assume appropriate supervisory responsibilities for independent contractors who are not separately registered as broker-dealers, we recognize that, in certain instances, SRO rules may not have been applied to all such independent contractors. In this connection, we also believe that it is important to emphasize that a simple denial of "control" of an independent contractor by a broker-dealer would not remove its responsibility for supervising that person. To the extent that a firm forms a relationship with an independent contractor, that firm would be responsible for either (1) ensuring that the independent contractor was registered as a broker-dealer or (2) assuming the supervisory responsibilities attendant to a relationship with an associated person. Therefore, the Commission believes that if a salesperson was not registered and a broker-dealer permitted him to hold out to the public that he was acting on behalf of that firm, such salesperson would be deemed to be an associated person of the broker-dealer.

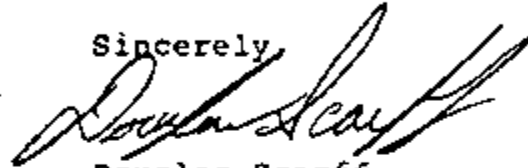
We are advising all the SROs of our views on this matter so that any necessary modifications in their rules and enforcement procedures which presently conflict with the Commission's position on the status of independent contractors under the Act can be

4/ Part I, Investor Protection, Hearings on H.R. 6789, H.R. 6793, S. 1642 Before a Subcommittee of the Committee on Interstate and Foreign Commerce, House of Representatives, 88th Cong., 1st Sess. 255 (1963).

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made. It should be noted that the Commission's position does not prevent a SRO from prescribing rules for its members which are more restrictive than the Act on how the relationship between a broker-dealer and its associated persons should be structured. I hope through the clarification of this matter that we are able to assure uniform application of the Act to every broker-dealer. In this regard, if you have any questions concerning independent contractors, please contact Sarah Ackerson at (202) 272-2857.

Sincerely,

A handwritten signature in cursive script, appearing to read "Douglas Scarff".

Douglas Scarff
Director