ADDRESS

of

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SECURITIES AND EXCHANGE COMMISSION

BEFORE

THE EASTERN GROUP

of

THE NATIONAL ASSOCIATION OF SECURITIES COMMISSIONERS

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It has been my pleasure to communicate with many of you through the mails, over the telephone or via Western Union; but this is the first opportunity I have had for an oral interchange of views with most of you. While it ill-behooves a federal official to speak otherwise than with reverence of the mails and the instrumentalities of interstate commerce, I must confess that a heart-to-heart talk appeals to me as a far more effective medium for the transmission of ideas. Consequently, I am indebted to this Group and, particularly, to its Chairman for inviting me to participate in this discussion of our mutual problems.

When the Securities Exchange Act of 1934 was enacted, the devices and contrivances employed on exchanges to separate the investor from his money had been exposed and publicized with some thoroughness. It was, therefore, feasible at the outset to project a fairly comprehensive plan of regulation for the exchange markets. Minimum standards of fair practice were specified in considerable detail by the Act, and the exchanges were brought directly under federal supervision through a program of registration which included an undertaking on the part of each exchange to comply and to enforce compliance by its members with the provisions of the Act and the rules promulgated thereunder.

The over-the-counter markets, however, presented a vastly different picture at that time. Authentic data concerning these markets were lamentably lacking. Comparatively little was known of their scope and character, the number and types of securities traded in, the technique of operations, the volume of transactions. Some of the more patent forms of abuse had, from time to time, been revealed through the efforts of the various state agencies and the post-office inspectors. The methods of the sell-and-switch operator, the bucketeer, the tipster-sheet publisher, the dynamiter and the high-pressure salesman, were familiar. But with respect to the more subtle

forms of manipulation and deceit -- many of them sharpened to a fine edge of perfection -- there was a conspicuous dearth of exact knowledge.

This lack of adequate information, coupled with the absence of any organized market mechanism, necessitated a different approach to the regulation of the over-the-counter markets from that which was possible in respect of the exchanges. As originally enacted, Section 15 merely authorized the Commission to prescribe rules which would insure to investors in the over-the-counter markets protection comparable to that provided by the Act in the case of organized exchanges. The problem of creating a blueprint and specifications was left with the Commission.

Here was a task worthy of one's mettle. Obviously, the most urgent and critical problem was to devise methods for exerting the full weight of federal authority against those persons who, by past performances, had manifested their unfitness to remain in the securities business. There are individuals in every walk of life who will adhere to no principle of decent conduct; who will shun the methods of fair and honorable business dealing in favor of the weapons of deception, fraud, pettifogging, cozenage and treachery. The expulsion of such individuals from the securities business has been one of the prime objectives toward which the Commission, since its inception, has directed its energies. It is our view that the business must be made "too hot" to hold them.

As a first step in the accomplishment of this objective, it was deemed essential that a system of registration be set up for all brokers and dealers whose activities brought them within the scope of federal jurisdiction. Here we had the advantage of precedent. Thirty-nine states had previously prescribed licensing or registration requirements for brokers and dealers and their number has since been increased to forty. Preliminary to the formulation of standards for admission to and exclusion from registration,

a careful analysis was made of the standards prevailing in the states. It was found that some of these could not be availed of, for the reason that federal jurisdiction in respect of over-the-counter transactions stems not from the police power, as in the states, but from the power to regulate the use of the mails and the instrumentalities of interstate commerce. Other grounds for disqualification prescribed by the state legislatures, while feasible of enforcement in their respective states, presented too gigantic an enforcement problem for a federal agency. After mature consideration of all the factors involved, the Commission adopted a program which provided for the denial of registration, if the public interest so demanded and the applicant or a key person in his organization had wilfully made a false statement in connection with his registration; or had been convicted within ten years of a crime connected with a securities transaction or the securities business; or was enjoined from any conduct connected with the purchase or sale of a security. Provision was also made for the revocation of registration for any cause which would have justified denial, or for wilful violation of the 1933 or 1934 Act, or for fraud in the conduct of the business of a broker or dealer.

The experience of the ensuing year so thoroughly demonstrated the practicability of this program that on May 27, 1936, its salient features were translated into statutory law by an amendment to the Securities Exchange Act. Under the amendment, a broker or dealer is prohibited from using the mails or the instrumentalities of interstate commerce to effect or induce any transaction over-the-counter unless he is registered with the Commission. An exemption from registration is provided for those whose business is exclusively intrastate. They, of course, are subject to the jurisdiction of the state commissions.

As of March 15, 1937, the Commission had permitted the registration statements of 6,585 brokers and dealers to become effective. The geographical distribution of these registrants may be of interest to you. New York, of course, leads the procession with 2,549 registrants, of which 2,060 have their principal offices in New York City. Illinois is second with 428; Massachusetts third with 360; California fourth with 352; and Pennsylvania fifth with 318. The rest are widely scattered. The distribution by regions is as follows:

New England	533
Middle Atlantic	3,231
South Atlantic	178
North Central	1,314
South Central	515
Mountain	242
Pacific	540
Outlying territories and possessions	32
Total effective registrations	6,585

To date, proceedings have been brought by the Commission to determine whether registration shall be refused or revoked in the case of 259 brokers and dealers. The proceedings have been completed in 226 cases and are pending in the remaining 33. The completed cases have resulted in the refusal of 18 registrations, the revocation of 6, the suspension of 3, and the withdrawal or cancellation of 71 "under the gun". Percentagewise, these proceedings have had the effect of eliminating persons from registration in more than 43% of the completed cases.

I have discussed at some length the genesis and development of our registration program not only to make clear its objectives and direction but to show how it dovetails with and supplements the program of the state commissions. In dealing with the undesirable and dangerous element in the securities business, it is idle for federal and state agencies to think in terms of competition with each other -- as idle as if members of different fire battalions were to debate which should turn its hose on a burning building.

The cooperation we have received from the state agencies in this connection has been of the most gratifying sort. There is a continuous flow of information between the Commission and the New York State Bureau of Securities. We have been furnished by the Pennsylvania Securities Commissioner with the details of refusal or revocation orders issued by him in not less than 80 cases. Our relations with other state agencies have been equally happy. On our side, we have compiled a tremendous amount of data concerning persons in the securities business which is available to state officials and other responsible agencies at all times. This interchange of information has been exceedingly wholesome and fruitful to everyone, except the individuals under investigation.

Ours is a never-ending task. There are no periods of slackwater where securities racketeers are concerned. They are elastic men who rebound from depressions, injunctions and even stretches in the penitentiary. Their ingenuity and resourcefulness ought not to be underestimated; and the gullibility of their victims frequently surpasses belief. Every advance in science, in industry, in transportation, in communication, brings them swarming to the scene as the heatherbell attracts the voracious bee. A shift in the government's monetary policy, a war scare, the repeal of the prohibition

amendment, the opening of a gold vein, the bringing in of a new gusher, the chain-letter fad, the supposed appetite of Italian soldiers in Ethiopia for frog legs -- all these have furnished opportunities for stock swindlers to endeavor to capitalize a wave of popular interest. Their depredations can be checked only by the united and unrelenting efforts of federal and state enforcement agencies with the assistance of reputable individuals and associations in the securities business and of public-spirited groups of citizens organized to combat fraud.

In addition to the need for continuous and cooperative effort in the field of enforcement, we are jointly confronted with the task of devising means for instilling in the investing public a healthy skepticism. The average investor, as all of you know, is likely to be incredibly naive. He is prone to rely upon promises and assertions, as distinguished from facts. He learns only after repeated and bitter experiences that the more sensational and extravagant the promises accompanying a solicitation to invest, the less substance those promises are likely to have. In the words of Sir Francis Bacon, "What a man had rather were true he more readily believes." The task of protecting the investor consists largely of awakening in him an insatiable thirst for cold, hard facts and arousing him to the dangers inherent in assigning his judgment to the keeping of others until their absolute integrity, responsibility and competence have been thoroughly demonstrated.

In the matter of defining and prescribing standards of fair practice, we likewise have a common responsibility. Some of the states have recently manifested a desire to bring their requirements, particularly in respect of the furnishing of information, more nearly in line with those of the Securities and Exchange Commission. We are, of course, always happy to furnish

them with such assistance as we can in the solution of problems which inevitably arise in connection with such a project. Certain areas of regulation deserve to be mentioned as presenting special opportunities for significant work by the state commissions. I refer particularly to the control of securities salesmen and investment counsel, who are not subject to the registration requirements of the Commission unless their activities bring them also within the definition of "broker" or "dealer".

One is struck, in examining the various state statutes, by divergences in their treatment of similar problems. Differences are observed in such fundamental matters as the powers vested in the enforcement agencies; the standards and forms prescribed for the qualification of brokers, dealers and salesmen; the standards and forms prescribed for the registration of securities; the methods by which securities may be registered; and the types of securities which are exempted from registration. The incidents of this lack of uniformity may bear more heavily upon reputable brokers and dealers than upon those who seek to circumvent the law. It may well be that organizations such as this can perform a great public service by thoroughly exploring the feasibility of rendering more nearly uniform the securities legislation of the various states, with due regard to local and regional conditions.

I trust that the emphasis I have placed on the need for coordinated activity in the field of enforcement will not be construed as reflecting an opinion that there is no room in the securities business for self-regulation. The types of abuse to which I have earlier referred can be dealt with only by the application of criminal and civil sanctions; for with men who lack conscience ethical sanctions are unavailing. I need hardly add that there are a great many men engaged in the securities business in whom a fine instinct for fair dealing is never absent. For them, as for us, the activities of the sub-marginal dealer present a spectacle painful to behold.

For them, as for us, the vitalization of principles of equitable practice is a matter of deep concern.

The Commission has frequently in the past expressed its sympathy with the principle of self-regulation in those areas where self-regulation can be made effective. The exchanges and other voluntary associations of brokers and dealers can demonstrate the efficacy of self-regulation by a wise and proper policy of self-discipline; by seeking to inspire in their members an abiding recognition of the grave responsibilities which are imposed by their important vocation; by articulating concepts of fair practice and encouraging the powerful application of those concepts to dealings throughout the industry; and by lending the full weight of their great influence to the elevation of the standard of business ethics beyond the point which legislation unaided can achieve.