SECURITIES REGULATIONS FOR THE DISTRICT OF COLUMBIA

HEARING

BEFORE A

SUBCOMMITTEE OF THE COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE HOUSE OF REPRESENTATIVES

EIGHTY-SEVENTH CONGRESS

SECOND SESSION

ON

DISCUSSION OF THE SECURITIES REGULATIONS FOR THE DISTRICT OF COLUMBIA

MAY 21, 1962

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SECURITIES REGULATIONS FOR THE DISTRICT OF COLUMBIA

MONDAY, MAY 21, 1962

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCE AND FINANCE OF THE
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D.C.

The subcommittee met at 10:30 a.m., pursuant to call, in room 1334, New House Office Building, Hon. Peter F. Mack, Jr. (chairman of the subcommittee), presiding.

Mr. MACK. The subcommittee will come to order.

This morning we have scheduled a hearing on the securities regulations in the District of Columbia. It has been called to the attention of this committee that there has been an unusual amount of questionable activity here in the District of Columbia.

The Securities and Exchange Commission and the National Association of Securities Dealers have taken certain action in recent months to correct the situation.

This committee feels that whatever action is necessary to solve the problem in the District should be taken. We recognize that the Securities and Exchange Commission has authority over vast areas, primarily interested in the regulation of securities on an interstate basis. But there does not seem to be any justification for having a situation existing right here in the Nation's Capital that is not regulated, to have an area which is not regulated, and to have situations existing here that are worse or as bad as any other areas of the country.

For that reason, we have scheduled the hearings today to determine what action should be taken to solve this problem.

Our first witness today will be Mr. William L. Cary, Chairman, Securities and Exchange Commission.

STATEMENT OF WILLIAM L. CARY, CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION; ACCOMPANIED BY MANUEL F. COHEN, COMMISSIONER; PHILIP A. LOOMIS, DIRECTOR, DIVISION OF TRADING AND EXCHANGES; ARTHUR FLEISCHER, LEGAL ASSISTANT TO THE CHAIRMAN; ALEXANDER J. BROWN, JR., ACTING REGIONAL ADMINISTRATOR, WASHINGTON REGIONAL OFFICE; AND STUART LAW, AN ATTORNEY IN THE DIVISION OF TRADING AND EXCHANGES

Mr. CARY. Mr. Chairman and members of the committee, I am William L. Cary, Chairman of the Securities and Exchange Commission.

I have with me my colleague, Commissioner Manuel F. Cohen, also Philip Loomis, the Director of the Division of Trading and Exchanges; my legal assistant, Arthur Fleischer; our Acting Regional Administrator of the Washington district, Alex Brown, and Stuart Law, an attorney in the Division of Trading and Exchanges.

I am here to testify on the problems of securities regulations in the District of Columbia. I have a prepared statement, which I believe you have copies of. I will expect to proceed through that with minor deviations.

The Commission believes that a serious problem existed in the Metropolitan Washington area with respect to the conduct, business methods, ethics, and qualifications of numerous broker-dealers engaged in the securities business.

This situation has been graphically and thoroughly discussed in a series of articles by Miriam Ottenberg in the Washington Star.

It has been reflected in the great number of enforcement actions brought by the Commission and the National Association of Securities Dealers against local firms; by the crescendo of illegal and unethical practices; by the number of local brokerage firms that have gone out of business; and by the substantial number of new firms managed by inexperienced personnel.

Apparently vigorous enforcement action has measurably reduced the present gravity of the situation, although we have no illusions it is entirely cured. We cannot be assured there will be no recurrence unless additional corrective action is undertaken. It is my understanding that a main purpose of these hearings is to assist in the determination of what such action might be.

I wish to point out that the problems of securities regulation in the District of Columbia are not unique. As the committee knows, the Commission is presently engaged in a broad study of the securities markets pursuant to Public Law 87–196, a bill introduced by Congressman Mack.

One of the important reasons for this study was evidence of a general breakdown of controls and lowering of standards in various sectors of the securities markets. The situation in the District of Columbia appears to represent a particularly intensified and extreme example of a national problem.

Why has there been an acute problem in the District?

I do not have any scientifically developed correlations. But I do believe that there are certain factors peculiar to the Metropolitan Washington area which aggravate problems normally present in securities regulation.

In the first place, the District of Columbia has no local securities regulation—no "blue sky" law. There are only two States without this type of legislation. Its absence in the District appears to have been a substantial inducement in encouraging both the formation of substandard new brokerage firms and the movement of undesirable persons from other areas to here. Convincing evidence is seen in the fact that nearly all new brokerage firms have located within the boundaries of the District, rather than in Maryland or Virginia.

Moveover, principals and salesmen from outside the District with so-called boilerroom backgrounds became participants in local firms. The District had become a haven for a developing breed—the migratory broker-dealer who flocks to the place of minimum interference with his operation.

I might say in that connection, there have been quite a few home-grown ones, too.

Secondly, the metropolitan area would generally be attractive to broker-dealers. Its comparatively high-income military and Government population, largely transient and allegedly somewhat unsophisticated in investing, and its large number of retired people, interested in supplementing fixed income, obviously present a prime target for unscrupulous brokers and their salesmen.

While this potential appears not to have been fully appreciated until recently, the phenomenal sprouting of local brokerage houses in the past few years attests to the fact that the possibilities offered by the market here have become well known. The new firms, some of which enjoyed rapid apparent growth for a time, in turn, trained new salesmen. Then the salesmen, upon exposure to the prospects offered, frequently opened up firms of their own.

The problems of securities regulation in the District of Columbia may be illustrated in numerous ways. The growth of the broker-dealer community in itself is exceptional.

At the end of 1958, there were 71 District firms who were members of the NASD. At the end of 1961, this number had increased over 47 percent to 104.

In this connection, it should be borne in mind that in the interim a large number of firms had failed—23 in 1961 alone. By contrast, the net gain in NASD membership for the Nation as a whole was only 22 percent—and the failures were correspondingly lower.

The genesis—and subsequent history—of many new firms reflects what has caused our anxiety and resulted in our actions. A staff study of the past 5 years shows that many local brokerage firms have been formed by persons formerly associated with houses that the Commission had closed.

Approximately one-third of the 67 that went out of business in the past 5 years had an officer, director, or owner who had previously worked for a firm against which the Commission had brought proceedings. Half of this group had two such persons.

As a dramatic instance of how substandard firms have grown, hydra-like, from the pieces of revoked firms, let me give the following example: A large District broker-dealer recently was put out of business by the Commission's Washington regional office. Investigation of possible fraud in the operations of this firm had barely begun when a number of salesmen and others connected with it opened new offices of their own.

Indeed, even before the firm closed, its salesmen were setting up firms. Altogether, at least 16 new houses were started by alumni of the original alma mater. Of this group, nine have either gone bankrupt, been forced to sell out, become dormant, or been put out of business.

Proceedings have been brought against several of this group of nine, and investigation is in progress with respect to others.

A barometer of what the District securities problem was may be seen in the great number of enforcement actions brought by the Commission and complaints filed by the NASD against District broker-dealers.

During the 4-year period up to June 30, 1959, a total of 12 administrative proceedings were brought by the Commission against District firms.

From July 1, 1959, to May 7, 1962, a period of less than 3 years, a total of 20 such proceedings were brought, nearly twice that of the previous period. Similarly, from July 1, 1955, to June 30, 1959, only two injunctive proceedings were brought against local firms.

From July 1, 1959, to May 7, 1962, 18 such actions have been brought, an increase of 900 percent. The Commission's Washington regional office has brought more of these actions against District brokerage firms than firms in all other States for which this particular regional office is responsible (Maryland, Virginia, West Virginia, Delaware, and Pennsylvania).

Data furnished to the Commission by the NASD is likewise illuminating. The NASD has indicated that, over the past 5 years, the number of complaints filed against District broker-dealers increased 650 percent, over three times the national increase of 215 percent.

Further, in 1960, the NASD filed complaints against 8 percent of its members nationally, whereas, for the District, the figure was 25 percent.

Thus, one out of four District firms was the subject of an NASD complaint involving some infraction of its rules. In 1961, possibly because of the increase in the number of local firms that went out of business, the District's percentage dropped to 18 percent, but this was still twice the number of complaints per member as the national percentage.

The number of local broker-dealer firms that have gone out of business is an additional measure of what has been the poor health of the broker-dealer community here.

Nationally, in 1961, approximately 8 percent of the firms admitted to the NASD failed. In the District, 18 percent of NASD member firms failed.

This rate of failure has presented a grave danger to the investing public and has resulted in substantial losses by many investors. One recent District broker-dealer, which is now in bankruptcy, has debts of well over $1 million, and few assets.

Hundreds of individual public investors dealing with this firm failed to receive certificates for which they paid, or proceeds from stock which they sold. It is doubtful whether they will receive anything on their claims filed in the bankruptcy proceedings.

There is evidence to demonstrate that these failing firms were characterized by management which had little or no prior experience. Such experience as existed was too frequently with a firm that had been involved in Commission proceedings.

Nearly half of the firms which commenced business in the past 5 years and failed had no executive with any previous experience except in a firm involved in revocation proceedings or injunctive action.

The consequences attendant upon minimal standards of qualification for the securities business—so graphic here—are the subject of major concern in the special study now being conducted by the Commission.

The unhealthy state of the securities business here in the District is also illustrated by the types of securities broker-dealers have been selling. In many cases, for example, the insiders and underwriters have taken for themselves what might appear to be an unconscionable amount of the proceeds of a public offering of securities and have left little for the benefit of the company and its public shareholders.

Thus, in one case, a company which had an operating deficit of over $12,000 was underwritten by a local broker. The total issue was for 150,000 shares at $2 per share. The underwriting group received 40 cents per share as commission and expenses and 30,000 shares of stock at a penny and a half a share, a total compensation of approximately $120,000 or 50 percent of the net proceeds received by the issuer.

Seven months after the stock was issued, the price had risen over 500 percent to more than $11 per share. The issuer is now the subject of bankruptcy proceedings.

In another case, the public paid nearly $175,000 for what eventually was a 30-percent interest in a company which had less than $3,000 in the bank, less than $200 worth of office furniture, and a net loss for the 6 months in which it had been in business of over $6,000. The insiders received the other 70 percent of the company for less than $500. The issuer is now bankrupt.

Securities problems in the District are perhaps most acutely demonstrated by the allegations, and evidence, of widespread fraudulent conduct on the part of certain local broker-dealers. Because of the Commission's quasi-judicial functions, it is not appropriate for me to comment on any pending cases or active investigations.

But, speaking generally, the erosion of standards which has occurred to some extent on a national level appears to have been magnified in the District. Just as the broker-dealers seem to have found a center of operations in the District, so have all of the unsavory practices which the Commission is constantly trying to extinguish.

The aforementioned conditions lead to the question of whether some type of legislative action is called for.

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The District of Columbia, unlike virtually all of the States, is without legislation of its own, and must rely on the Federal securities laws for protection.

In this connection, it should be emphasized that, as a practical matter, investors in the Maryland and Virginia suburbs are affected by the situation in the District, inasmuch as the "blue sky" laws of these States do not effectively reach District brokers.

The Commission has attempted to meet the challenge of the problem without any new legislation. We have taken concentrated enforcement action in this area, which I believe has been at least temporarily productive in diminishing the unhealthy practices and creating a new environment.

Some of the specific steps that we have taken include the following:

(1) The assignment of personnel to the Washington regional office from the national office and other regional offices.

(2) The institution, since January 1, 1961, of 23 administrative and injunctive proceedings against District broker-dealers, involving a total of 79 persons from the local area, and 23 parties from other areas.

Indicative of the complexity of these administrative cases is one pending broker-dealer proceeding involving some eight firms, including four local ones, and some 20 salesmen and principals, of whom 9 are from the Washington area. Another case new pending took over 9 months to investigate.

(3) Various investigations are in the final stages. It is anticipated that a number may result in reference for criminal prosecution to the U.S. attorney, Mr. David C. Acheson, who is giving us his full cooperation.

However, despite the important steps we have taken and the apparent general improvement in the conduct of local broker-dealers, the situation still presents many difficulties—which can be expected to increase to the extent that the market for over-the counter securities moves up.

Vigorous enforcement can never be a permanent substitute for high regulatory standards. If there is a relaxation of our present efforts, and our national enforcement responsibilities might make this necessary, there could be a renaissance of past unsavory practices, hopefully now substantially curtailed.

The Federal securities acts do not presently appear to be a full answer. The legislative history and the language of the Federal statutes make clear that they are not, and were not intended as, complete instruments for local regulation.

They contemplate concurrent jurisdiction by the Securities Commission of any State or the District of Columbia. Although specifically designed to supplement, rather than supplant, local securities legislation, the Federal acts have been forced to function in the District of Columbia as a local "blue sky" law without the provisions which "blue sky" laws normally have.

Under the Federal acts, the Commission's power is largely punitive or remedial, not preventive. There are only limited controls over entrance into the securities business.

Usually, we cannot act until violations have taken place, and investors have suffered—until the fraud has been committed, or the firm's net capital depleted beyond the limit allowed by law.

Further, revocation and suspension proceedings before the Commission, and injunctive and criminal actions filed by the Commission in Federal courts, necessarily must follow prescribed procedures and meet high standards of proof which, in turn, frequently delay appropriate action and impose a heavy burden on our staff.

By contrast, local "blue sky" administrators ordinarily have far greater control over those desiring entry into the business. Character or experience requirements may be imposed as they may not under the Federal law as it presently stands.

Furthermore, the administrators may exercise summarily many enforcement powers. Frequently, registration of securities is required, with controls over unconscionable transactions.

The Commission does not believe it can achieve the full degree of securities regulation—realized in other jurisdictions with local regulation—through continuation of its present intensive enforcement program without impairing its ability to meet our national responsibilities.

Accordingly, the Commission recommends that some further regulator powers over broker-dealers in the District of Columbia be established.

Several alternatives are open:

(1) The District of Columbia is presently exploring the extent of its power under its licensing statute, section 47–2344, to license broker-dealers and establish standards with respect to character and capital. If adequate standards can be developed in this manner swiftly, we shall be hapy to work with the District authorities. However, they have indicated substantial doubts as to the extent of their authority under the existing licensing statute. Furthermore, rules are not enough, and experienced personnel would have to be available to the District for the administration of any rules.

Finally, under the District Code, the only penalty for operating without a license appears to be a fine up to $300 or imprisonment for not more than 90 days.

While conviction for such a violation, being a misdemeanor in the securities field, would probably be a ground for a broker-dealer revocation by this Commission, we believe it would be much more effective if the local authorities themselves could put an unlicensed securities firm out of business.

(2) Another possibility is to have local broker-dealers regulated by the Commission acting as a "blue sky" administrator. Expanded SEC jurisdiction could be effected by an amendment to section 15 of the Securities Exchange Act of 1934, which would provide rule-making power in the Commission with respect to broker-dealers doing business in the District of Columbia.

This power would permit the Commission to establish standards for qualification of broker-dealers and their salesmen with respect to net capital, character and experience. It would also give us increased powers for taking immediate action to suspend operations of a firm.

(3) We believe the preferable solution is a strong "blue sky" statute for the District of Columbia to be administered under the District of Columbia Government by an administrator with an adequate enforcement staff.

Such a statute could be based upon the uniform "blue sky" law, which offers several alternatives as to statutory provisions.

The act followed a 2-year study of State legislation. Part 1 of the Uniform Act prohibits fraud in the sale or purchase of any securities. Part 2 provides for the registration of broker-dealers and their salesmen, and of investment advisers.

Included in this part are sections dealing with denials, suspensions, and revocations. If control of securities issues is desired, part 3 provides three alternative methods for registration: by notification, by coordination, or by qualifications.

It should be noted that this legislation has various provisions for payment of fees which presumably could be set at a sufficiently high amount to permit adequate agency staffing.

The Commission recommends a local "blue sky" statute with local administration for several reasons.

If the Congress desires that local government in the District should be strengthened, it would seem appropriate for the District to have its own "blue sky" laws and "blue sky" administrator. All but two States have such a law and feel it necessary to regulate the conduct of brokers and dealers doing business in their jurisdiction. To the extent that the present District problem arises from a lack of local legislation, it would seem proper for the District to have a law and build a staff in order to meet future recurrence of the present problem.

Most importantly, I must emphasize that the Commission's responsibilities are national. As I have stated, we accelerated our enforcement program in the District of Columbia, and I believe that this action has produced noticeable results and created a change in the environment here. However, if we were to continue our activities on the same intensive basis, this concentration would tend to impair our national enforcement obligations.

Similarly, we prefer not to assume a particular responsibility with respect to a region where we regard our main job to be one of establishing national standards. Indeed, in many ways, this would divert us from the primary program to which we are committed—as evidenced by our market study, which was initiated by this very committee.

Many of the issues apparent in the District situation are being studied as national problems. By way of example, an important aspect of the market study is an analysis of the qualification, training, supervision, and financial responsibility of broker-dealers and their salesmen. Our studies might lead us to the conclusion that present requirements for entrance into the securities business should be strengthened. If that be so, we would then properly be meeting a problem, apparent not only in the District, but on a national basis.

At the same time, I want to emphasize our belief that any new Federal legislation will not, and should not, supersede local regulation. They should be concurrent.

Were the Commission to assume the responsibility of local regulation, we would, in effect, be administering two different types of laws—one based on the "blue sky" pattern and the other based on the national pattern.

The confusion that would be created, and the anomalous picture that would be presented, of a single agency administering two different sets of rules is evident. The same person who was unfit for the

securities business under District standards might become fit federally upon moving across Eastern Avenue to Silver Spring.

Furthermore, the Commission is reluctant to assume normal "blue sky" controls over securities issuers. These controls often go beyond the Federal reliance on full disclosure and may entail the power to pass on the merits of issues—for example, whether the compensation to the underwriters or insiders is exorbitant. Clearly, here the assumption of another type of power could only engender difficulties.

The creation of a strong District "blue sky" administration would help plug the existing gap in securities regulation. Virginia has the Uniform Securities Act and Maryland has recently adopted it.

Suburban investors could lodge complaints with the District authority, and District investors with the two State administrators. It is likely that the several administrators would be able to work in close cooperation. And, of course, the Commission itself would continue to carry on its present function of enforcing the Federal securities laws in all three jurisdictions, thus giving an added layer of investor protection.

I should like to point out here that the above considerations militate against exercise of our present rulemaking powers so as to adopt special regulations for the District of Columbia.

Under present law, we could undoubtedly issue particular rules with respect to the District under the Securities Act of 1933. That would be with respect to new issues of securities.

However, there may be some question as to our power to single out local broker-dealers under the Securities Exchange Act of 1934. Furthermore, our powers under the Exchange Act are limited; by way of example, we cannot impose character and experience requirements as a condition to entry into the securities business. Moreover, if we single out the District because problems develop here, would we not have the obligation to give individual treatment to other areas to the extent they manifest serious problems of securities regulation? We feel obligated to operate on a national basis and exercise of our present rulemaking authority for the District would raise all the problems attendant upon dual regulation.

We recognize that, to some extent, the establishment of a local securities authority might appear unnecessarily in light of the presence of the Commission itself here, as well as the existence of a Washington regional office. Shortrun budgetary savings might be effected if the Commission assumed the powers of local regulation, rather than a separate agency. However, in the long run, a disproportionate part of our budget might end up in being allocated to regional problems at the expense of our nationwide program.

Moreover, as I have attempted to demonstrate, local regulation in many respects differs from that contemplated by the Federal securities laws. It would seem anomalous for us to exercise one type of power regionally and another nationally. Most importantly, our emphasis has been, and should be, on national standards and national enforcement.

Accordingly, the Commission recommends the enactment of a "blue sky" law for the District of Columbia to be administered by a local administrator. This action would undoubtedly assist in meeting the local securities problems, would be consistent with our traditional

Federal pattern of dual regulation, and would permit our continued concentration on national problems.

In conclusion, I might just add that I am not trying to say that the "blue sky" law will completely eliminate the problem, but it will help in the process and, of course, we will be operating concurrently with it.

That is the end of my prepared statement, Mr. Chairman.

Mr. MACK. Thank you, Mr. Chairman. You have devoted a lot of time to this problem and we appreciate having your detailed statement on this matter.

Mr. Chairman, this problem is not completely new, is it? It has been existing for a number of years.

I recognize and appreciate the fact that you pointed out—that it has become almost uncontrollable in the last 3 years. At least we have had a tremendous number of violations and questionable activities, violations of ethical standards, in the last 3-year period.

But I am wondering if any thought has been given or if the question has been raised as to why we have not dealt with this matter at some point within the last 28 or 29 years since the Securities and Exchange Act was passed.

Mr. CARY. Mr. Chairman, I agree with you that the problem of the District of Columbia has always been one which the Commission has faced. I do not think it has been of the gravity that would warrant, for example, a special and major effort until the last few years.

We had a staff, back in January 1957, of 14 for the regional office, and that covered, by the way, not only the District of Columbia but Virginia, West Virginia, Maryland, Delaware, and, I believe, Pennsylvania. It seems, relatively speaking, that vis-a-vis those other areas, larger in size, most of the problems of the regional office have concentrated in the District and, indeed, have demanded more of our personnel. The local office has expanded at the moment, I believe, up to about 30.

During this past period, should we have put more people to work on District problems or ought we to have been thinking about special rules for the District? I would say that we are always having to put out fires in various areas; relatively speaking, I do not think the District was regarded as a major area requiring special consideration until the past 3 or 4 years.

Mr. MACK. Mr. Chairman, I concluded from your statement that you prefer a local "blue sky" law for the District of Columbia?

Mr. CARY. Yes, Mr. Chairman.

Mr. MACK. The question I want to raise is this: Was this necessary 25 years ago, or did it just develop in the last 3 years?

Mr. CARY. Mr. Chairman, we have made some inquiry and found that there was some legislation introduced in Congress concerning a "blue sky" law for the District of Columbia around 1933, when the Securities Act of 1933 was passed.

So far as I know, nothing happened after the introduction of the bill. We cannot find its legislative history and do not have very much information concerning it.

I am quite sure you are correct that the need for a "blue sky" law in this jurisdiction, as in the only two others now that do not have such a law, may have been apparent over this period.

I doubt whether the need for local regulation became as crucial until this recent period. Therefore, it is only now that we have really come out and taken a public position on this.

Mr. MACK. You have also, evidently, had a opportunity to research it, and there has not been legislation introduced since that time to provide a "blue sky" law for the District?

Mr. CARY. Not to our knowledge; no, sir.

Mr. MACK. That would have been 28 or 29 years ago.

Mr. CARY. I think there has been a vehicle for this in recent times, Mr. Chairman, which was not available earlier; namely, the Uniform Securities Act, which has been very carefully prepared and offers alternative forms which can be used in enacting such a law.

Mr. MACK. I just have one final question at this time.

Do you feel that your District office, your representatives here, have devoted their time to protecting the investors here in the District of Columbia during this quarter of a century when they should have been interesting themselves on interstate matters?

Mr. CARY. That is a pretty hard question to give a sure answer to.

I will say that up to this time we have had a fairly limited number of people working exclusively on District of Columbia matters. I think personnel has been divided up, more or less in proportion to the need existing at any particular time. For example, the problems in New York, or in the Far West during the uranium period, as their seriousness became evident, justified a larger allocation of our personnel.

Therefore, without being positively sure of the accuracy of my answer in view of the fact that I have only been at the Commission for a year and a month, I would say that there has been a fairly reasonable allocation according to enforcement needs at any particular time.

A good deal more manpower, of course, has been needed in the District during the past 3 years.

Mr. MACK. Would you agree, though, that your personnel, when they concentrate on the District problem, are quite successful in improving the situation?

Mr. CARY. I think the problem has been reduced in magnitude. As I say, I won't assure you that it won't come up again. To some extent it is abated because the condition of the over-the-counter market now is such that perhaps there has been a little less enthusiasm for sales in that area in the District.

Thus, under those conditions, I would say at the moment it has been reduced and abated, but I do not want to say it has been cured, by any means.

Mr. MACK. Then, if it was improved following the time that your enforcement officers came in, there must have been some violations there at the time when it was not being rigidly enforced?

Mr. CARY. Major violations; yes, sir. In one example which I gave it appears that investors have lost a very substantial amount of money. This demonstrates, perhaps, the usefulness of the "blue sky" approach. We do not have the so-called suspensory power that a "blue sky" Commissioner has. In the event that he finds evidence of actual dereliction he just closes a firm down and holds the hearing subsequently. We do

not have that power. We have to have a suspension proceeding prior to taking any action with respect to the firm.

Mr. MACK. Mr. Hemphill?

Mr. HEMPHILL. Thank you, Mr. Chairman.

Mr. Chairman, may I first say as a member of the subcommittee I have been most happy in noting the progress of your administration. I congratulate you and the members of your Commission.

I gather from your statement that there is some doubt in your mind as to whether or not, under the 1934 act, the Commission has jurisdiction in the District of Columbia. Is that correct?

Mr. CARY. To enact special rules with respect to the District of Columbia; yes, generally.

Mr. HEMPHILL. As I understand it, the authority of your Commission is based on the interstate commerce feature of the transaction. That is the elementary principle, that these stock transactions are interstate commerce?

Mr. CARY. That is correct.

Mr. HEMPHILL. The 1933 act defines interstate commerce for purposes of your jurisdiction as among or between the States or within the District of Columbia?

Mr. CARY. Yes, sir.

Mr. HEMPHILL. It has been pointed out to me by our able staff that that is in section 2, subparagraph 7, of the act?

Mr. CARY. Yes, sir.

Mr. HEMPHILL. Then, in the 1934 act, section 3, subparagraph (a), subparagraph 16, defines a State as including or meaning the District of Columbia. But the next paragraph defines interstate commerce as among the several States.

If we pass some legislation here which definitely gives the Commission the rulemaking power within the District of Columbia and leaves no doubt about it, how far will that go in curing the situation which your presentation this morning seeks to cure?

Mr. CARY. Well, sir, if I could divide the question up. As you have indicated, our jurisdiction is broader under the Securities Act of 1933 with reference to the District than under the Securities and Exchange Act of 1934. Certain sections of the 1933 act also undoubtedly give us the power to single out transactions in the District—particularly with respect to new issues of securities. This would not touch the broker-dealer problem, but only the distribution of securities.

I doubt whether we could have a whole different registration process with respect to the District. I have no doubt that we could have perhaps a firmer set of regulations with respect to what we call the Regulation "A" type of issuance, those offerings less than $300,000. But I am skeptical whether further regulation of new issues would meet the problems here that we have previously indicated. It would only meet them on a very narrow base, and in a very limited area.

You are quite right, further, that our powers are not as broad with reference to the District of Columbia under the Securities and Exchange Act of 1934.

Perhaps we have not exercised our rulemaking power under the Securities and Exchange Act of 1934 with reference to the whole country as much as perhaps we should and shall.

At this moment, out special study is trying to determine, to what extent, for example, should we, through legislation on the one hand, or through using our rulemaking powers on the other, raise the qualifications for entrance in the securities business.

What if you gave us a special broad power under the Exchange Act with reference to the District of Columbia. That would give us a mandate to go ahead and make rules more broadly in the District than we could elsewhere.

Under the present statute, I thing there might be a question of power whether we could regulate certain activities here and not with respect to the whole country—on a disuniform basis.

But if you gave us that mandate, we could undoubtedly do it.

If you gave us powers, (1) with respect to qualifications of broker-dealers, and (2) even the suspensory power of the type I referred to, undoubtedly, it would help.

We would have to increase our manpower. We could exercise the power given by those rules to meet some of these problems. But we prefer to have the District problem handled by a "blue sky" administrator—we hesitate to pick out this area and operate, you might say, more as a day-to-day policeman, when, in fact, we think our big function is one of making rules that will cover the Nation.

Our big function, for example, in the case of the exchanges, is to see that those exchanges carry out their responsibilities; at the same time to work with the NASD—in other words, to supervise all those institutions organized for the purposes of self-regulation.

Therefore, we do not deny that the powers that you might choose to give us might not help the situation. But we think our job should be on the national level and that we should not be operating in the District in one way and the rest of country in another way. Accordingly, those powers that you refer to would better be in the hands of a "blue sky" administrator with whom we are working concurrently, just as they are in other States.

Mr. HEMPHILL. I had in mind asking a question perhaps giving you the elasticity to not only make the regulations apply nationwide, but to zero in on any given area by the power which you would have, and that would include the District of Columbia, which is a source of much concern to me because we have so many people here apparently who want local authority and are a little power-drunk with the idea.

If we create another commission here, it is another commission, something else to worry about. I am not against the proposal, but I hesitate to create something else here in the District which in my humble opinion, has deteriorated so as the Nation's Capital with the growth of more local authority.

Mr. CARY. This question of zeroing in on the District and not having the power to zero in on the other areas is not quite what we would like.

We think that we ought to be operating on a national level. With the limited manpower we have, and the problems that are beginning to develop in our special study, I think we are going to be operating at a maximum burden in approaching each of the problems on a uniform and national basis.

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Mr. HEMPHILL. My use of the term "zero in on the District" was not a play on semantics, I meant if we gave the powers not only to zero in on the District the unquestionable authority which the act of 1934 does not give to your satisfaction, but to zero in on any other area of the country.

It appears to me if you ever zero in on the District of Columbia, or if you needed to zero in on New York, Florida; once you have done that, you are going to set the pattern in these day of communication.

It seems to me if you went into a place and cleaned it up, and threw these people out of business that are in the wrong business, took away their licenses or right to do business, from the national standpoint you could prohibit them from going back into business in Virginia, Florida, or any other place?

Mr. CARY. May I ask our Director of the Division of Trading Exchanges to comment on that further? He may have some idea I had not thought of.

Mr. LOOMIS. If I understood the question, it appeared to be a suggestion that the Commission might be given greater powers which it could exercise anywhere whenever it thought there was a particular problem in a particular area.

That might be of assistance in the District, and perhaps in some other places. It would produce, perhaps, the problems the chairman mentioned, of our treating different parts of the country in different ways, which, for a national agency, may present some questions.

I think in response to certain of the earlier questions asked, as an example of the problems that occur when you zero in on a particular area, that in the last year or so our Washington office has had to concentrate so on the problems of the District of Columbia that maybe our coverage in certain other parts of this region has not been all that we would like to see.

That is another aspect of the problem.

Mr. HEMPHILL. Suppose we broaden the definition of interstate commerce with reference to the 1934 act so that it would be unquestioned that you had the authority within the District of Columbia.

The District of Columbia is a creature of the Congress. Congress has power over interstate commerce and over the definitions of it. At least, the courts have said that. Once we have done that, then you have all the authority you need; is not that correct?

Mr. LOOMIS. I am not quite sure. Our problem as to broker-dealers in the District and perhaps elsewhere is not so much finding jurisdiction in the sense of interstate commerce, because most broker-dealers do use the mails.

The mails are instrumentalities of interstate commerce. It is rather that the nature of our powers in connection with broker-dealers, as the chairman pointed out, are sort of punitive rather than preventive and remedial.

We do not have any power, even with regard to a broker-dealer in interstate commerce, to pass upon his character or require him to have a certain amount of experience, which powers "blue sky" Commissions commonly exercise.

So I am not sure that merely changing the definition of interstate commerce would fully meet the broker-dealer problem in the District.

Mr. HEMPHILL. Thank you very much.

Mr. MACK. Mr. Keith?

Mr. KEITH. Thank you, Mr. Chairman.

Are there any other areas which are without any supervision of the sort which result in "blue sky" laws? I am thinking particularly of military installations.

Mr. CARY. First of all, sir, in respect of the jurisdictions in which there is no "blue sky" legislation, those are only Nevada and Delaware. As to the application of "blue sky" laws on military installations, I have not given that any thought.

Is there any problem with respect to the application of the "blue sky" law on a military reservation?

Mr. LOOMIS. That has been somewhat uncertain. There are some military installations, though I think it is a minority of them, where it is contended that they are exclusively Federal areas in which the State authority does not extend.

On the other hand, most military commanders have precluded, by order, the sale of securities on the reservation in violation of the laws of the particular State in which the installation is located.

I suppose that the particular problem for military installations, from the viewpoint of the "blue sky" law, arises in connection with the installations in foreign countries where, of course, no State laws apply.

Mr. KEITH. Your hearings downtown have indicated that there are some abuses in this kind of installation. I think it might be appropriate for you to give the committee a memorandum as to your recommendations as to how, from a jurisdictional point of view, that situation might be improved.

Mr. CARY. Yes, sir; we will be glad to do so.

Let me say in general, with respect to this situation, that it is true that there have been, in our hearings, some evidence of salesmen—who are in the military—selling to military.

I suppose the greater problem that we have noticed is the use by salesmen here in the District of the Pentagon telephone book. In other words, calling people in the Pentagon and getting in touch with the military who, as a group, might constitute a source of potential securities customers.

We will be glad to consider this particular problem. It may well be, Congressman Keith, that it becomes more significant in view of the statement made in the newspaper I noticed this morning—in perhaps which you have reference to—about the establishment of brokerage firms in military installations abroad.

Mr. KEITH. Along the same line, are there any other areas where there is a lack of jurisdiction and a need for such supervision? For example, the Panama Canal Zone, or the Virgin Islands, how are they regulated?

Mr. CARY. I will have to ask Mr. Loomis to speak to that point.

Mr. LOOMIS. There is not any local regulation that I know of either in the Panama Canal Zone or in the Virgin Islands.

I frankly have not encountered many problems in the securities field in those areas. Particularly, I would not think there would be much in the Virgin Islands, because of the nature of the community there. There has been a problem which has been of some concern—

the Chairman alluded to it—in regard to securities sales on major military installations in Europe, where the local requirements, whatever they are, are deemed inapplicable.

There is no State jurisdiction. We cannot effectively reach the situation. I think that to some degree, however, the regulation of these activities probably has to be in the hands of the military themselves, the command, who can, of course, give such orders as they see fit regarding the securities sales.

Mr. KEITH. That is all, Mr. Chairman.

Mr. MACK. Mr. Hemphill?

Mr. HEMPHILL. Something just occurred to me. I followed you as you presented your statement. On page 13, you have a numeral 3:

> We believe the preferable solution is a strong "blue sky" statute for the District of Columbia, to be administered under the District of Columbia government by an administrator, with an adequate enforcement staff.

Where does this committee have jurisdiction of that?

Unless we broaden the definition of the 1934 act, where we would have any jurisdiction? Suppose we pass legislation that is suggested here, creating the authority in the District of Columbia? I do not know whether we have the right to do it in the first place.

In the second place, if we did create it, we would lose authority over it, which the District of Columbia Committee would attain.

Mr. CARY. I believe I agree with you in this sense: As I look at it, this committee is analyzing a problem in the securities field for which it is responsible. If our suggested proposal that the District adopt a "blue sky" law be thought appropriate, then I think legislation along those lines would probably fall or might fall within the District of Columbia Committee of Congress.

Therefore and on this point you certainly know much better than I—I would suppose you would not have jurisdiction over the functions of that "blue sky" administrator, just as you do not over the "blue sky" administrators of the various States.

But I think the basic question that we are discussing here is what kind of an organization or what kind of a law should you have to meet a problem which clearly falls within your jurisdiction; namely, dereliction, fraudulent conduct, and the other securities problems in the country and specifically in the District.

Mr. HEMPHILL. I hate to think of what would happen to the poor fellow when the morning newspaper here got through with him. Down home we call the Washington Post the Daily Worker, the Washington Daily Worker.

We have seen them castigate people whose intentions were so honorable that it was almost fantastic to see the lengths to which they would go to castigate someone who is trying to do their job.

That causes me concern because I want to be of help to your Commission. I have a legislative responsibility to try to be of help.

Thank you.

Mr. MACK. Mr. Chairman, on page 4 of your statement you refer to this problem of the salesman going into business after your Commission has put the broker-dealer out of business.

I believe Mr. Loomis has referred to this problem in his testimony before your special committee. Is this a matter which is not limited to the District of Columbia, but which is a problem throughout the

entire country, or is Mr. Loomis referring specifically to the District of Columbia?

Mr. CARY. The case that I was referring to is a problem which could happen throughout the country, and I think Mr. Loomis, in his testimony before the special study, was likewise speaking to that problem.

For example, we might enjoin a firm, but then in order to put the individuals who are salesmen in the firm out of business, we would have to go through a revocation proceeding of the broker-dealer firm which might take as much as 3 years or so, and at the same time, in that revocation proceeding find these persons to be so-called willful violators or causes.

Under those circumstances, once they are causes, then they would not be in a position to work for any other firm or organize their own without our approval.

But until the salesmen are found to be causes, there would not be a basis for disqualifying them at the present time under the existing laws. It is that kind of question, of course, that we have to examine on a broad scale in the special study.

Mr. Loomis might want to make a comment further on this.

Mr. LOOMIS. I think that the instance that I referred to in my testimony before the study is the same one that the Chairman referred to in his statement on page 4.

On the other hand, as the Chairman has said, this is a thing that can happen outside the District, and there have been instances of it. Perhaps not as dramatic mathematically, but definitely instances of it in other parts of the country.

Mr. MACK. This could happen in States which do have "blue sky" laws?

Mr. CARY. Yes, it could. Although, of course, a "blue sky" administrator, having the suspensory power, might be able to put a particular person out of business immediately if he found that there was a basis for it in the light of his past conduct or financial history or background.

Mr. MACK. But these new firms would also be registered with you as brokers?

Mr. CARY. The new firms would be registered with us; yes, sir.

Mr. MACK. And they would be members of the National Association of Securities Dealers?

Mr. CARY. They might be or they might not be. I might ask Mr. Loomis whether he knows whether most of those would have become or did become members of the NASD.

Mr. LOOMIS. I would suppose that most of them would have at least applied and may well have become members. As the Chairman pointed out, while we took action against the firm, we did not have then time to make a case against each salesman in the firm and prove that he, individually, violated the law.

Mr. MACK. Could I interrupt to ask if you ever do that?

Mr. LOOMIS. Yes, we do it on occasion.

Mr. MACK. On rare occasions?

Mr. LOOMIS. Well, we have tried it both ways. In New York, where this problem arose, we would sometimes proceed against all the salesmen.

As the Chairman says, this makes a very complicated trial, with 20 respondents, each of them having his own attorney, and all wrapped up in one case it can go on for years. We have sometimes tried to move faster against the firm and pick up the salesmen later.

Mr. MACK. Mr. Chairman, do you feel there is any necessity or justification for additional legislation to deal with this problem, or is this one of the matters that you presently have under study with your special investigation?

Mr. CARY. I would say, sir, that this is a matter which we have presently under study. Therefore, I cannot speak to any immediate concrete legislation. It certainly is a matter which was clearly involved in the public hearings which we have been holding in the last 2 weeks.

Mr. MACK. Then this problem nationally will be dealt with, undoubtedly, in your report?

Mr. CARY. It will be; yes, sir.

Mr. MACK. On page 7, you refer to the underwriting group. An underwriting broker had a deficit of $12,000.

Mr. CARY. Yes, sir. It is the company, not the brokerage firm. It is the so-called issuer.

Mr. MACK. The issuer had the deficit of $12,000?

Mr. CARY. Yes, sir.

Mr. MACK. Then, the underwriting group received $120,000, or 50 percent, of the proceeds received by the issuer?

Mr. CARY. Yes, sir.

Mr. MACK. Do not you or the NASD have rules concerning the amount of commissions charged?

Mr. CARY. In answer to that, first of all, we do not. What we do, under the Securities Act of 1933, is to force disclosure of that on the front page of the prospectus.

In other words, we bring it to light so that it is clearly known.

Mr. MACK. That is with regard to the 30,000 shares?

Mr. CARY. That would be the 30,000 shares, and that would be the 40 cents per share as well. All of that would be clearly spelled out. But that is all we would do at this time.

The NASD, on the other hand, has moved ahead in the last year, specifically, and is beginning to study these problems of underwriters' compensation, and are taking some action in that area.

It is an area, by the way, in which we, ourselves, are doing further study in connection with the special study.

Mr. MACK. But you have no rules regarding either the minimum or the maximum commission?

Mr. CARY. No, sir. Generally, not at all.

Mr. MACK. You mentioned there are two other States that have no "blue sky" laws. Do those two States rely on the Federal Government for enforcement and regulation of securities?

Mr. CARY. Those two States, sir, are Nevada and Delaware. I would say the answer in general is yes.

Now, whether or not their attorney general operates under just a general fraud provision which he might interpret broadly, I cannot speak. But I would say, in general, that, or the regulation of securities selling is primarily left in the Federal Government's hands.

Mr. MACK. Do you have any problems in those two States similar to the ones you have in the District of Columbia?

Mr. CARY. I think in view of the fact that I have only been here a year, I might ask Mr. Loomis to speak to that question.

Mr. LOOMIS. We have not had any particular problem in regard to Delaware. I am not quite sure why, but there has not been much that has come to our attention. We have from time to time had enforcement problems in Nevada, as elsewhere.

But, of course, Nevada is not a metropolitan State. It is a small State, spread out over a wide area, and there is less likely to be a concentration of securities activity there. In fact, there is not. But we have had our problems from time to time.

Mr. MACK. Do you have a regional office in Nevada?

Mr. LOOMIS. No, sir. We have an office in San Francisco and a branch of that in Los Angeles. Nevada is handled out of the Los Angeles branch, primarily.

Mr. MACK. Would you need additional legislation for the Securities and Exchange Commission to act as the "blue sky" law administrator?

Mr. CARY. Of the District of Columbia?

Mr. MACK. Yes. The "blue sky" administrator for the District.

Mr. CARY. Yes. To exercise full "blue sky" powers in the District, we would need additional legislation. Our question is whether we should establish rules for the District of Columbia which we have not established yet for the other parts of the country?

Mr. MACK. My point is you would need additional authority other than the amendment to section 15 of the Securities and Exchange Act?

Mr. CARY. If there were amendments to section 15, I think that would be enough to give us substantial authority. It would not give us authority over issues of securities, but perhaps that would not be necessary.

Mr. MACK. Do you feel that that would give you authority that would be necessary to substantially eliminate the practices now engaged in in the District of Columbia?

Mr. CARY. If it were the choice of the Congress to place this responsibility on the Securities and Exchange Commission, we think that we would receive adequate powers under certain amendments to section 15 to the 1934 act.

Mr. MACK. I thank you, Mr. Chairman, for your testimony. I do feel that some action needs to be taken here in the District of Columbia. At least, I have been somewhat favorable to granting additional authority to the Securities and Exchange Commission. But if some other action is forthcoming that will solve the problem, we might defer to the other organization or group that made the proposal.

Mr. CARY. Thank you, Mr. Chairman.

Mr. MACK. Our next witness is Mr. Wallace Fulton, executive director, National Association of Securities Dealers.

STATEMENT OF WALLACE H. FULTON, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC., ACCOMPANIED BY MARC A. WHITE, COUNSEL, AND RICHARD PETERS, SECRETARY OF THE ASSOCIATION'S DISTRICT NO. 10

Mr. MACK. Mr. Fulton, we are happy to welcome you again before the Commerce and Finance Subcommittee.

I know you have been quite familiar with the problem existing here in the District of Columbia.

We will be happy to have your testimony at this time.

Mr. FULTON. Thank you very much, Mr. Chairman.

Mr. Chairman and members of the subcommittee, I am Wallace H. Fulton, of Washington, D.C., executive director of the National Association of Securities Dealers, Inc.

I have with me Marc A. White, counsel, and Richard Peters, secretary of the association's district No. 10 which includes Washington, D.C.

We are here to discuss securities regulations for the District of Columbia designed to protect the public in the purchase and sale of securities. The need for corrective measures arises, in part, from the great increase of broker-dealers in the Washington area in the immediate past, coupled with the lack of regulations applicable locally to protect the public from the dishonest or the grossly inexperienced securities dealer.

I have stated in the past that the District of Columbia would benefit from additional regulations, provided they are properly administered.

Most State securities laws have three major classifications. These are: (1) the area of registration and licensing of broker-dealers and salesmen, (2) the registration of securities, and (3) establishment of provisions having to do with fraud.

Any consideration of additional regulations for the District of Columbia should be made with a recognition that the Federal securities acts are administered in Washington and all broker-dealers in the District must be registered with the Securities and Exchange Commission.

All new issues of securities sold must be registered with the Commission or offered under a regulation A exemption obtained through the regional office of the Commission, also located in Washington.

Proceedings based upon violations of the Securities Act, which include fraud, are instituted by or at the behest of the Securities and Exchange Commission.

Thus, the two of the three areas covered in any State securities law seem to be amply covered by present laws. The one feature of certain State laws not covered relates to registration and licensing of broker-dealers where the requirements in a given State are greater than those now in effect for registration with the Securities and Exchange Commission.

It should be recognized that no salesman registers as such with the Commission.

Thus, there would appear to be a need for regulation to set certain standards for entry into the business as a dealer or as a registered representative which do not exist in the District of Columbia. Such

additional requirements and standards may relate to minimum capital, prior experience, education, and character.

In connection with the administration of any regulation, I believe that the Securities and Exchange Commission should be the administering power because of its expertness in the field and the present existence of a regional office which, in my opinion, is competent to handle the problems of registration, to hold proceedings on revocations or denials of registration and related activities.

It would not, however, be difficult to organize a competent local administration if a law were to be adopted for the District of Columbia. In some States which have securities laws, their administration may be inadequate if legislatures do not appropriate the necessary funds.

In other words, if an adequate job is to be done here, it will require money and, above all, experienced personnel.

It is hoped the SEC study group functioning under House Joint Resolution 438 will make recommendations to the Commission and Congress for national standards for entry into the securities business, and these standards would be applicable to the District of Columbia.

In summary, I suggest that regulations for securities dealers who operate in the District of Columbia be adopted and be administered by the Securities and Exchange Commission.

I realize that this means additional work for an already hard-pressed agency, but it would seem that the Commission is the ideally suited body with the existing capabilities to perform this service.

Mr. MACK. Does that conclude your statement?

Mr. FULTON. That concludes my statement, Mr. Chairman.

Mr. MACK. Mr. Hemphill?

Mr. HEMPHILL. Thank you, Mr. Chairman.

What effort, if any, have been made by our association to police this problem in the Washington area?

Mr. FULTON. The percentage of members examined by the association in 1960—the association as a whole was 33 percent.

In district No. 10, and that is this district, including North Carolina, Virginia, Maryland, and the District of Columbia, 56 percent; in Washington, D.C., 64 percent.

In 1961, the comparable figures were association 31 percent; district No. 10, 62 percent; and Washington, D.C., 107 percent. Several members were reexamined during the year.

So far this year we have examined 13 percent of our members in Washington, D.C.

Of the 29 new members from Washington, D.C., in 1960, 20 had been examined by April 5, 1961. On the average, the 20 were examined 4½ months after becoming members. But this figure ranges from 2 months to 11 months.

Of the 27 new members in Washington, D.C., in 1961, 15 had been examined by December 31, 1961. On the average, the 15 members were examined within 5 months from the date of membership. This figure ranges from 1 to 6 months.

Of the 10 new members from Washington, D.C., in 1962, 3 had been examined by April 30, 1961. These three members were examined within 1 to 3 months of membership.

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Examinations are assigned selectively, based on the secretary's knowledge of the members' type and business activity.

Now, as to complaints which came about as a result of these examinations, in 1960, district No. 10 ranked fourth in total number of complaints filed.

In 1961, district 10 ranked fourth, again. The first four, district 12, New York, district 7, district 8, the Middle West, and district 10, this district 30.

As of April 30, 1962, District 10 ranked fifth.

In Washington, D.C., we filed in 1960, 25 complaints as of the percentage of members examined. In 1961, 18.3 percent, and in 1962, so far, 7.7 percent.

From another view, in 1960—this is the percentage of members, the first one, and the next one is the percent of examinations—21.6, 17.3, and this year, 24.2.

In 1960, 1961, and 1962, we expelled 29 members of the association from the District of Columbia. Last week, the district committee met and four were expelled by action of the district committee, which action, of course, will not become final because they have the right to appeal to the board of governors and from there to the SEC.

So I think it is right to say, it is fair to say, that quite a bit has been done in the way of examinations of these members by the association, and there have been resulting complaints and decisions, resulting in pretty drastic penalties.

Mr. HEMPHILL. If 1 of those 29 that your association suspended set up his own shop and began doing business in securities, as I understand it, the most he could be fined is $300; is that correct? What could be done to him?

Mr. WHITE. I think, Congressman, that $300 figure relates to the penalty section of the District of Columbia laws. Our penalties range from censure to a fine of $1,000 per violation, to a suspension from membership, and to an expulsion.

If your question relates to the effect on people in a firm, when we expel a firm, if we name the principals, officers, and salesmen implicated in the violations, we normally revoke their registration, if that penalty fits the dereliction.

If we name them as a cause of the expulsion, under our bylaws, article I, section 2 of the bylaws, they cannot come back into the business as principals or as salesmen unless they go through a membership continuance procedure set up under the law and are finally approved by the Securities and Exchange Commission.

Mr. HEMPHILL. That is what I wanted to know.

Thank you very much.

Mr. MACK. Mr. Fulton, what would be the situation if you and the District government recommend that the Securities and Exchange Commission have this responsibility, and the Securities and Exchange Commission feels that the District government should have this responsibility?

Does that mean that we should not change the law in either direction?

Mr. FULTON. No, Mr. Mack; I do not think so. I think the law should be changed and I think it can be changed without much difficulty, to give the Commission the power, as Mr. Cary stated on page 12 as one of his alternatives.

The expanded jurisdiction could be affected by an amendment to section 15 of the Securities and Exchange Act of 1934, which would provide rulemaking power in the Commission with respect to broker-dealers doing business in the District of Columbia.

That is our position exactly expressed by Mr. Cary in his No. 2 alternative. We think it is the thing to do.

Mr. MACK. Is there need for additional legislation besides the amendment to section 15 of the Securities and Exchange Commission Act?

Mr. FULTON. In my opinion, no.

Mr. MACK. Do you feel that if the amendment is adopted, the Commission will then be in a position to fully protect the investors in the District of Columbia?

Mr. FULTON. I think if an appropriate amendment is adopted, that the Commission could act as a "blue sky" administrator and would accomplish that which could be accomplished by an independent administrator, operating under the District of Columbia law.

Mr. MACK. On page 1, you stated:

> I have stated in the past that the District of Columbia would benefit from additional regulations, provided they are properly administered.

Were you then referring to the amendment to the Securities and Exchange Act?

Mr. FULTON. The inference is "Yes." That is correct.

Mr. MACK. Were you referring to the Securities and Exchange Commission when you mentioned, "provided they are properly administered"?

Mr. FULTON. Yes, because I think the Securities and Exchange Commission could properly administer the law.

Mr. MACK. You think that they would?

Mr. FULTON. I think they would, yes.

Mr. MACK. Were you implying that if the District government had the same authority they might not properly administer it?

Mr. FULTON. No, I am simply saying they do not have the experience.

Mr. MACK. If the Congress decided not to amend the Securities and Exchange Act to give them this rulemaking authority, then would you favor some type of legislation to provide for a "blue sky" law here for the District of Columbia?

Mr. FULTON. Yes, if Congress decided not to give the Commission that power.

Mr. MACK. Are you in a position to state whether you have a similar problem in Delaware and Nevada?

Mr. FULTON. No, we do not have a problem in Delaware, and I have no knowledge of a problem in Nevada.

We have very few members in Nevada, and very few in Delaware.

Mr. MACK. In other words, you do not have the volume of business in those two States; is that correct?

Mr. FULTON. That is correct.

Mr. MACK. I have one further question.

I recall in previous testimony a representative of your group said that they are obligated to permit anyone or practically anyone to become a member of the NASD.

Is that a true statement?

Mr. FULTON. That is correct. There are only certain so-called statutory bars which, if they exist, would act to prohibit, or we could then refuse to allow that person against whom the bars exist to become a member of the association.

Mr. MACK. By law?

Mr. FULTON. Yes, sir; by law.

Mr. WHITE. We have certain prohibitions to the entry into business on the part of a member and of an individual. They are granted under section 15(a) of the Securities and Exchange Act of 1934.

Those bars are that a person where action has been taken against him by the Commission, by us, or by a stock exchange, which has revoked his license, operates as a permanent bar to membership in the association.

There are additional standards. If an individual was found guilty of a misdemeanor or a felony in connection with the securities business, or he was found guilty of a misdemeanor or felony in connection with fraudulent conversion, embezzlement, and so forth.

Unless a person falls within those particular areas, he must be admitted to membership under the act under which the association is registered.

Mr. MACK. Then, under present law, you have no way of keeping out the undesirable members who have been involved in an operation similar to the one referred to by the chairman on page 4 of his statement?

Mr. FULTON. If those people have had their registration revoked by the Commission, that acts as a statutory bar.

Mr. MACK. But all their salesmen seem to be free to come over and join your association.

Mr. FULTON. That is absolutely correct, unless they have been named.

Mr. WHITE. In our actions, Mr. Chairman, we name as many individuals who we think are implicated in the alleged violations. If we take an action which either revokes their registration or names them as a cause of the expulsion, if the final action is expulsion, we have a bar, a disqualification under our bylaws to prevent their reentry.

In the Commission's actions, if they name a person as a cause of the action, that operates as a bar, too. As I understood the Chairman of the Commission's testimony and that of Mr. Loomis, to be that in some cases they do name these people. In others, because of the difficulty of proof, they do not.

Mr. MACK. Then, it would be more difficult for them to name them than for your organization?

Mr. WHITE. I think that is a correct statement.

Mr. FULTON. I think so, yes.

Mr. MACK. Are you familiar with the case to which they referred this morning?

Mr. FULTON. Yes, we are familiar with that case.

Mr. MACK. Did the NASD take any action prior to the time that the Commission revoked the registration?

Mr. PETERS. Yes, sir.

Mr. MACK. Did your association make any reference to the salesmen?

Mr. PETERS. We revoked the principal officers.

Mr. MACK. But not any of the representatives?

Mr. PETERS. Not on that particular action, but on subsequent ones we did.

Mr. MACK. You did subsequently?

Mr. PETERS. Yes, sir.

Mr. MACK. This is with regard to different broker-dealers but not to the representatives of this broker-dealer?

Mr. PETERS. That is correct.

Mr. MACK. Mr. Keith.

Mr. KEITH. Thank you, Mr. Chairman.

We met with you, Mr. Fulton, I think, last summer.

Mr. FULTON. That is correct, Mr. Keith.

Mr. KEITH. You spent some time with us on the details of an instant which I will identify as the *Late Tape* incident. Do you recall?

Mr. FULTON. Yes, I remember it now. The incident of a registered representative, whose registration had been revoked by us and who then appeared in southern California performing the same sort of operations as he had performed in Florida, and which were very successful so far as he was concerned.

Mr. KEITH. Yes. In trying to recall the circumstances, this owner of the *Late Tape*, the yacht, put into Los Angeles Harbor and had a dinner party for acquaintances and others who were registered brokers, and during the course of this dinner party one of the friends of the owner left the table and completed a phone call and returned and related the substance of the phone call, which pertained to a rather large offering of stock that was available.

During an interchange of information there was a lot of enthusiam shown by the owner of the boat. The next day, these eight or nine dinner guests moved into the market and picked this stuff up, causing the market to rise substantially.

This was the kind of thing which you illustrated could happen amongst your membership, and you used it as an illustration of how the association was on its toes and alerting its membership to this kind of thing so it would not happen again; is that correct?

Mr. FULTON. Mr. Keith, the people who became enthusiastic were young, somewhat inexperienced, registered representatives of member firms of the association, who were induced to put orders in for the purchase of this stock through their respective firms, and they did so.

Apparently, the gentleman who had chartered the yacht—we have since learned that he did not own it—then unloaded his own securities as the market went up as a result of these buying orders.

We have alerted our members to that effect.

Mr. KEITH. If I remember rightly, you then said he went to San Francisco and did the same thing?

Mr. FULTON. He did, that is correct. And then he went to France. I do not think he is back.

Mr. KEITH. About how long ago did this take place?

Mr. FULTON. It took place last year.

Mr. KEITH. When the committee went out to California, I was fascinated by this story. I was asked to luncheon by the board of directors of the San Francisco and Los Angeles branches of the West Coast Exchange, and I asked about this incident. Not a one of them could recall having heard of it.

They went out and checked during the luncheon to see if there was anybody else that had heard of it. There seemed to be a failure of communications in this particular respect.

Mr. FULTON. It does not surprise me that the directors of the Pacific Coast Stock Exchange did not know of that situation.

Mr. KEIRH. Is it that they are not members of your association?

Mr. FULTON. Practically all of them are.

Mr. KEITH. Was there a failure of communication?

Mr. FULTON. There was no reason to communicate with them because the securities were over-the-counter securities and were not securities listed on the Pacific Coast Stock Exchange.

Mr. KEITH. I thought you said earlier that you had advised the west coast membership of this?

Mr. FULTON. Our own district committee, which is entirely separate from the Pacific Coast Stock Exchange group, and the members involved, of course. There was a very complete study made.

Mr. KEITH. That is all, Mr. Chairman.

Mr. MACK. Mr. Hemphill, have you anything else?

Mr. HEMPHILL. No, Mr. Chairman.

Mr. MACK. To make it clear, you feel that the amendment to the Securities Act would solve the problem here?

Mr. FULTON. I happen to believe that it would; yes, sir.

Mr. MACK. Mr. Fulton, I want to thank you for your testimony today.

Mr. FULTON. Thank you, Mr. Chairman.

Mr. MACK. Mr. Milton D. Korman, Assistant Corporation Counsel, District of Columbia.

STATEMENT OF MILTON D. KORMAN, PRINCIPAL ASSISTANT CORPORATION COUNSEL, DISTRICT OF COLUMBIA. PRESENT ALSO FROM THE DISTRICT GOVERNMENT: IRVING BRYAN, CHIEF, AND ROBERT F. KNEIPP, ASSISTANT CHIEF, LEGISLATION AND OPINIONS DIVISION, OFFICE OF THE CORPORATION COUNSEL; JOSEPH J. ILGENFRITZ, DIRECTOR OF LICENSES AND INSPECTIONS; AND C. T. NOTTINGHAM, SUPERINTENDENT, LICENSE AND PERMIT DIVISION, DEPARTMENT OF LICENSES AND INSPECTIONS

Mr. KORMAN. Thank you, Mr. Chairman. With me is Mr. Kneipp, the Assistant Chief of our Legislation and Opinions Division of the Office of the Corporation Counsel.

Also with me is the Chief of that Division, Mr. Irving Bryan, and the Director of the Department of Licenses and Inspections of the District, Mr. J. J. Ilgenfritz, and the Superintendent of the Division of Licenses and Permits of that Department, Mr. Nottingham.

Mr. MACK. We are glad to have you with us, gentlemen.

Do you have a statement to present?

Mr. KORMAN. No, I do not have a prepared statement, Mr. Chairman. I came at the invitation of the committee to be as helpful as I can and to tell you what we have done.

Mr. MACK. Maybe I can start out by asking you whether or not the District Commissioners have recommended any type of "blue sky" legislation to the Congress?

Mr. KORMAN. Categorically answering that, sir: No, they have not. I might tell you what has been done in the last few months.

Mr. MACK. I wanted to also say that the Securities and Exchange Commission this morning indicated that they felt that was the proper course.

Mr. KORMAN. I heard the testimony of Mr. Cary, the Chairman of the Securities and Exchange Commission.

I gathered from his testimony, Mr. Chairman, that he thought that was one of several ways of approaching this problem, and one which he probably favored. But I also gathered from his testimony that they would not be adverse to assuming the responsibility if it was the wisdom of the Congress that they should do so.

Mr. MACK. I think that is true. He indicated that he would carry out the laws that are enacted by the Congress. But I also had the distinct impression that he was not all enthusiastic about the enactment of such legislation, and that he preferred the enactment of legislation which would establish a "blue sky" law for the District of Columbia.

Mr. KORMAN. I think that is what he said, sir. I cannot deny that. I believe, however, that he was fearful of certain situations, about which I do not think he need have the fears that he anticipates.

One, it seemed to me that he was saying that the Securities and Exchange Commission would thereby be entering a local field, and that this was something that Federal agencies generally did not do.

I would call his attention, and the committee's attention, to the fact that there are quite a few instances where Federal agencies undertake to police and to regulate local situations in the District of Columbia.

One is the Federal Trade Commission, which I believe has a specific section devoted to the enforcement of the laws which they enforce in the District of Columbia.

The Comptroller of the Currency, for instance, has control of the local banks, in addition to his national duties. The Bureau of Federal Credit Unions, which is part of the Department of Health, Education, and Welfare, has, by law, supervision over the local credit unions in the District of Columbia, not only those that operate under the Federal credit union law, but also those that operate under the District of Columbia credit union law.

Mr. MACK. I imagine if Mr. Cary were here, he might want time for rebuttal. I am sure he would mention such things as your Public Utilities Commission that you operate in the District.

You have dual jurisdiction in several areas, dual agencies in several areas, with the Federal agencies, wherein you have the jurisdiction over the District of Columbia.

Mr. KORMAN. I do not understand how the Public Utilities Commission here would conflict with any Federal regulation.

Mr. MACK. We have an Interstate Commerce Commission which has similar responsibilities nationwide, and you have the Commission, which has the responsibility within the District of Columbia, such as the Illinois Commerce Commission has.

Some States refer to them as railroad commissions and in other States they are utility commissions.

Mr. KORMAN. We, of course, do not attempt locally to regulate interstate commerce. That was a purely local thing in the beginning, for a local concern.

I am not saying that it is impossible.

Mr. MACK. You do not have the authority to regulate interstate commerce but you do have the authority to regulate intrastate commerce?

Mr. KORMAN. Yes, sir.

Mr. MACK. Whether they have done a good job or not, that is what they have tried to do.

Mr. KORMAN. I am not saying that it could not be done, but what I was pointing out was that there are instances of Federal agencies regulating in the District of Columbia, the local conditions.

Mr. MACK. Let me ask this: Has the Commission given any consideration to the possibility of recommending a "blue sky" law for the District?

Mr. KORMAN. My understanding of the wishes of the Board of Commissioners of the District are these: That subsequent to the series of articles by Miss Ottenberg, which are generally referred to as the "Investors Beware" series, and which have been put out in pamphlet form, the Commissioners directed the Office of the Corporation Counsel to investigate to see whether or not there was power in the Commissioners to take any action without legislation, and to report to them on how to take action to correct some of the conditions and situations described in this series of articles.

If they have not been made a part of the record, I would offer them, Mr. Chairman, the articles that were the predicate for this.

(A reprint of "Investors Beware" may be found on p. 49.)

Mr. KORMAN. To do something about that, we summoned—well, not summoned, but requested—to come to our office representatives of various groups that we thought might be helpful to us, and as a result, we have had several meetings with, as best I can recall, these groups represented: The Better Business Bureau of the District of Columbia; the National Association of Securities Dealers; the Washington, D.C., Securities Dealers & Traders Association; the Securities and Exchange Commission—Mr. Loomis and, at another time, Mr. Lesh of that Commission attended our meetings.

Incidentally, Mr. Peters, who was here this morning with Mr. Fulton, attended several of our meetings on behalf of the National Association of Securities Dealers.

Also, the Superintendent of our Department of Licenses and Permits; the Director of the Department of Licenses and Inspections; the U.S. Attorney's Office of the District of Columbia, represented by its principal assistant; the Metropolitan Police Department, represented by a deputy chief and one other man; the Investment Bankers Association of America; and, of course, the Corporation Counsel, myself as principal assistant, and several other assistants.

There were representatives of several of the larger securities dealers in the District of Columbia, among them Landrum Allen & Co., Johnston Lemon & Co., and some others.

We discussed this problem at some length and attempted to see what could be done within the framework of the authority of the District Commissioners.

It was the consensus of all those who attended the meeting that some regulation was necessary to take care of the evils that had been described in this series of articles.

We found, and it is our belief, that the District Commissioners have at present limited authority which might or might not—probably would not—solve all the problems.

The extent of their authority at the present time, as we see it, is to require licenses of dealers or agents or both, and to possibly prescribe some limitations on those who might be licensed by providing that they must show some experience, they must be able to demonstrate trustworthiness by being under the tongue of good report, by not having been convicted of crime on prior occasions—certain limitations of that sort.

This might, by having them screened by our police department before licensing, which might be another proviso, screen out some of the people that have been entering the business here and doing some of the things that have been described in these articles.

We cannot be sure that it will take care of all the situations.

It was indicated that probably the most important thing that should be done was to have those who wanted to enter the business either show that they had been engaged in it elsewhere and had not been in difficulty—that is to show experience in the business for a certain period of time—or that they should pass an examination in order to be licensed.

The District of Columbia has no facilities for giving such an examination or grading it. Indeed, we have not the expertise in our organization to do these sorts of things. We would have to hire people for that.

The National Association of Securities Dealers offered to conduct such examinations and grade them for us, but under the law we cannot accept their services gratis, and we do not have funds to pay them with. We would have to have authority from Congress to do that.

After reviewing the situation, and Mr. Kneipp having prepared a very rough draft for discussion purposes only of what might be called a limited "blue sky" law for the District of Columbia, having taken the Uniform Securities Act that was mentioned here earlier this morning, changing it in some respects to apply to the District—and I have for the committee some of the drafts that went out, together with our letter of invitation that went to these people I mentioned to come to the meeting, or come to one of our meetings—we have discussed that at the meetings and have concluded that to do this would, of course, require legislation, and the setting up of a separate department in the District, or a new division in our Department of Occupations and Professions, which is a separate Department from the Licensing Department.

(The document referred to follows:)

GOVERNMENT OF THE DISTRICT OF COLUMBIA,
OFFICE OF THE CORPORATION COUNSEL,
Washington, D.C., April 24, 1962.

DEAR MR. ———: I attach the first draft of proposed regulations governing persons engaged in the business of dealing in securities, prohibiting fraudulent practices in relation thereto, and requiring the licensing of broker-dealers, agents, and investment advisers. Please note that this draft has been adapted from the Uniform Securities Act, accommodated to the deletion of part III of such act, relating to the registration of securities.

The attached first draft should be considered as a gross adaption of the Uniform Securities Act since the draft contains a number of provisions which the Commissioners, under existing law, are not authorized to adopt. These provisions have, however, been included in the attached draft for purposes of discussion, and for determination as to whether any recommendation should be made to the Commissioners that they sponsor legislation authorizing them to adopt some or all of such provisions.

I am having a meeting in my office, room 329, District Building, 14th and E Streets NW., at 2:30 p.m. on Monday, April 30, 1962, to discuss the attached proposed regulations. I would very much aappreciate it you could be present. If you find you will be able to attend this meeting, please bring with you the attached material.

Sincerely yours,

CHESTER H. GRAY,
Corporation Counsel,
District of Columbia.

DRAFT NO. 1, APRIL 20, 1962

(Uniform Securities Act adapted as District of Columbia licensing regulations after accommodation of such act to the deletion of Part III: Registration of securities)

Subject: Regulations governing persons engaged in the business of dealing in securities, prohibiting fraudulent practices in relation thereto, and requiring the licensing of broker-dealers, agents, and investment advisers.

Ordered, That the following regulations governing persons engaged in the business of dealing in securities, prohibiting fraudulent practices in relation thereto, and requiring the licensing of broker-dealers, agents, and investment advisers in the District of Columbia, are hereby adopted and promulgated.

INTRODUCTION

SECTION 1. SCOPE.—These regulations to regulate the activities of persons engaging in the business of dealing in securities, to prohibit fraudulent practices in relation thereto, and to require the licensing of broker-dealers, agents, and investment advisers, are adopted in accordance with the authority vested in the Commissioners of the District of Columbia by section 7 of the Act approved July 1, 1902 (32 Stat. 622), as amended (title 47, ch. 23, D.C. Code, 1961 ed.).

PART I—FRAUDULENT AND OTHER PROHIBITED PRACTICES

SEC. 101. SALES AND PURCHASES.—It shall be unlawful for any person licensed under the authority of these regulations, in connection with the offer, sale, or purchase of any security, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud;

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

SEC. 102. ADVISORY ACTIVITIES.—(a) It shall be unlawful for any person licensed under these regulations who receives any consideration from another person primarily for advising the other person as to the value of securities or

their purchase or sale, whether through the issuance of analyses or reports or otherwise—

(1) to employ any device, scheme, or artifice to defraud the other person; or

(2) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon the other person.

(b) It shall be unlawful for any investment adviser to enter into, extend, or renew any investment advisory contract unless it provides in writing—

(1) that the investment adviser shall not be compensated on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of funds of the client;

(2) that no assignment of the contract may be made by the investment adviser without the consent of the other party to the contract; and

(3) that the investment adviser, if a partnership, shall notify the other party to the contract of any change in the membership of the partnership within a reasonable time after the change.

Clause (1) does not prohibit an investment advisory contract which provides for compensation based upon the total value of a fund averaged over a definite period, or as of definite dates or taken as of a definite date. "Assignment", as used in clause (2), includes any direct or indirect transfer or hypothecation of an investment advisory contract by the assignor or of a controlling block of the assignor's outstanding voting securities by a security holder of the assignor; but, if the investment adviser is a partnership, no assignment of an investment advisory contract is considered to result from the death or withdrawal of a minority of the members of the investment adviser having only a minority interest in the business of the investment adviser, or from the admission to the investment adviser of one or more members who, after admission, will be only a minority of the members and will have only a minority interest in the business.

(c) It shall be unlawful for any investment adviser to take or have custody of any securities or funds of any client if—

(1) any provision of these regulations prohibits such custody; or

(2) in the absence of any such provision in these regulations, the investment adviser fails to notify the director that he has or may have custody.

PART II—REGISTRATION OF BROKER-DEALERS, AGENTS, AND INVESTMENT ADVISERS

SEC. 201. LICENSING REQUIREMENTS.—(a) It shall be unlawful for any person to transact business in the District as a broker-dealer or agent unless he is licensed in accordance with the requirements of these regulations.

(b) It shall be unlawful for any broker-dealer or issuer to employ an agent unless such agent is licensed in accordance with these regulations. The licensing of an agent shall not be effective during any period when he is not associated with a particular broker-dealer licensed in accordance with these regulations or with a particular issuer. When an agent begins or terminates a connection with a broker-dealer or issuer, or begins or terminates those activities which make him an agent, the agent as well as the broker-dealer or issuer shall promptly notify the Director.

(c) It shall be unlawful for any person to transact business in the District as an investment adviser unless—

(1) he is licensed in accordance with these regulations;

(2) he is licensed in accordance with these regulations as a broker-dealer without the imposition of a condition under section 204(b)(5); or

(3) his only clients in the District are investment companies as defined in the Investment Company Act of 1940 or insurance companies.

(d) Licenses issued in accordance with the provisions of these regulations shall be valid for the twelve-month period beginning on November 1 of each year, unless revoked, or suspended and not restored within such period.

SEC. 202. LICENSING PROCEDURE.—(a) A broker-dealer, agent, or investment adviser may obtain an initial or renewal license by filing with the Director an application together with a consent to service of process pursuant to section 314(g). The application shall contain whatever information the Director requires concerning such matters as—

(1) the applicant's form and place of organization;

(2) the applicant's proposed method of doing business;

(3) the qualifications and business history of the applicant; in the case of a broker-dealer or investment adviser, the qualifications and business history of any partner, officer, or director, any person occupying a similar status or performing similar functions, or any person directly or indirectly

controlling the broker-dealer or investment-adviser; and in the case of an investment adviser, the qualifications and business history of any employee;

(4) any injunction or administrative order or conviction of a misdemeanor involving a security or any aspect of the securities business, and any conviction of a felony; and

(5) the applicant's financial condition and history.

The Director may require an applicant for initial license to publish an announcement of the application in one or more newspapers of general circulation published in the District. If no denial order is in effect and no proceeding is pending under section 204, the license for which application has been made shall become effective at noon November 1 or the thirtieth day after application is filed, whichever occurs later in any license year. The Director may specify an earlier effective date, and he may defer the effective date until noon of the thirtieth day after the filing of any amendment. Licensing of a broker-dealer automatically constitutes the licensing of any agent who is a partner, officer or director, or a person occupying a similar status or performing similar functions.

(b) Every applicant for initial or renewal licensing shall pay a filing fee of $ in the case of a broker-dealer, $ in the case of an agent, and $ in the case of an investment adviser. When application is denied or withdrawn, the Director shall retain $ of the fee.

(c) A licensed broker-dealer or investment adviser may file an application for the license of a successor, whether or not the successor is then in existence, for the unexpired portion of the license year. There shall be no filing fee.

(d) The Director may require a minimum capital for licensing broker-dealers and investment advisers.

(e) The Director may require licensed broker-dealers, agents, and investment advisers to post surety bonds in amounts up to $10,000, and may determine their conditions. Any appropriate deposit of cash or securities shall be accepted in lieu of any bond so required. No bond may be required of any licensee whose net capital, as defined in these regulations, exceeds $25,000. Every bond shall provide for suit thereon by any person who has a cause of action under section 310 and, if the Director by rule or order requires by any person who has a cause of action not arising under these regulations. Every bond shall provide that no suit may be maintained to enforce any liability on the bond unless brought within two years after the sale or other act upon which it is based.

SEC. 203. POSTLICENSING PROVISIONS.—(a) Every licensed broker-dealer and investment adviser shall make and keep such accounts, correspondence, memorandums, papers, books, and other records as the Director may require. All records so required shall be preserved for three years unless the Director finds that particular types of records must be kept for a greater or lesser time than three years.

(b) Every licensed broker-dealer and investment adviser shall file such financial reports as may be required by these regulations.

(c) If the information contained in any document filed in accordance with these regulations is or becomes inaccurate in any material respect, the licensee shall promptly file with the Director a corrected amendment unless notification of the correction has been given under section 201(b).

(d) All the records referred to in subsection (a) are subject at any time or from time to time to such reasonable periodic, special, or other examinations by the Director, within or without the District, as the Director deems necessary or appropriate in the public interest or for the protection of investors. For the purpose of avoiding unnecessary duplication of examinations, the Director, insofar as he deems it practicable in administering this subsection, may cooperate with the securities administrators of other states, the Securities and Exchange Commission, and any national securities exchange or national securities association registered under the Securities Exchange Act of 1934, as amended.

SEC. 204. DENIAL, REVOCATION, SUSPENSION, CANCELLATION, AND WITHDRAWAL OF LICENSING.—(a) The Director is authorized to deny, suspend, or revoke a license issued under the authority of these regulations if he finds (1) that such action is in the public interest and (2) that the applicant or licensee or, in the case of a broker-dealer or investment adviser, any partner, officer, or director, any person occupying a similar status or performing similar functions, or any person directly or indirectly controlling the broker-dealer or investment adviser—

(A) has filed an application for licensing which as of its effective date, or as of any date after filing in the case of an order denying effectiveness, was incomplete in any material respect or contained any statement which was, in light of the circumstances under which it was made, false or misleading with respect to any material fact;

(B) has willfully violated or willfully failed to comply with any provision of these regulations;

(C) has been convicted, within the past 10 years, of any misdemeanor involving a security or any aspect of the securities business, or any felony;

(D) is permanently or temporarily enjoined by any court of competent jurisdiction from engaging in or continuing any conduct or practice involving any aspect of the securities business;

(E) is the subject of an order of the Director denying, suspending, or revoking his license as a broker-dealer, agent, or investment adviser;

(F) is the subject of an order entered within the past five years by the securities administrator of any State, or by the Securities and Exchange Commission denying or revoking registration as a broker-dealer, agent, or investment adviser, or the substantial equivalent of those terms as defined in these regulations, or is the subject of an order of the Securities and Exchange Commission suspending or expelling him from a national securities exchange or national securities association registered under the Securities Exchange Act of 1934, or is the subject of a United States Post Office Fraud Order; but (i) the Director may not institute a revocation or suspension proceeding under clause (F) more than one year from the date of the order relied on, and (ii) he may not enter an order under clause (F) on the basis of an order under a State act unless that order was based on facts which would currently constitute a ground for the order under this section;

(G) has engaged in dishonest or unethical practices in the securities business;

(H) is insolvent, either in the sense that his liabilities exceed his assets or in the sense that he cannot meet his obligations as they mature; but the Director may not enter an order against a broker-dealer or investment adviser under this clause without a finding of insolvency as to the broker-dealer or investment adviser; or

(I) is not qualified on the basis of such factors as training, experience, and knowledge of the securities business except as otherwise provided in subsection (b).

The Director may by order deny, suspend, or revoke any license if he finds (1) that the order is in the public interest and (2) that the applicant or licensee—

(J) has failed reasonably to supervise his agents if he is a broker-dealer or his employees if he is an investment adviser; or

(K) has failed to pay the proper filing fee; but the Director may enter only a denial order under this clause, and shall vacate any such order when the deficiency has been corrected.

The Director may not institute a suspension or revocation proceeding on the basis of a fact or transaction known to him when licensing became effective unless the proceeding is instituted within the next thirty days.

(b) The following provisions govern the application of section 204(a)(2)(I):

(1) The Director may not enter an order against a broker-dealer on the basis of the lack of qualification of any person other than (A) the broker-dealer himself if he is an individual or (B) an agent of the broker-dealer.

(2) The Director may not enter an order against an investment adviser on the basis of the lack of qualification of any person other than (A) the investment adviser himself if he is an individual or (B) any other person who represents the investment adviser in doing any of the acts which make him an investment adviser.

(3) The Director may not enter an order solely on the basis of lack of experience if the applicant or licensee is qualified by training or knowledge, or both.

(4) The Director shall consider that an agent who will work under the supervision of a licensed broker-dealer need not have the same qualifications as a broker-dealer.

(5) The Director shall consider that an investment adviser is not necessarily qualified solely on the basis of experience as a broker-dealer or agent. When he finds that an applicant for initial or renewal licensing as a broker-dealer is not qualified as an investment adviser, he may by order condition the applicant's licensing as a broker-dealer upon his not transacting business in the District as an investment adviser.

(6) The Director shall provide for an examination, which may be written or oral or both, to be taken by any class of or all applicants, as well as persons who represent or will represent an investment adviser in doing any of the acts which make him an investment adviser.

(c) The Director may by order summarily postpone or suspend licensing pending final determination of any proceeding under this section. Upon the entry of the order, the Director shall promptly notify the applicant or licensee, as well as the employer or prospective employer if the applicant or licensee is an agent, that it has been entered and of the reasons therefor, and that within fifteen days after the receipt of a written request, the matter will be set down for hearing. If no hearing is requested, and none is ordered by the Director, the order will remain in effect until it is modified or vacated by the Director. If a hearing is requested or ordered, the Director, after notice of and opportunity for hearing, may modify or vacate the order or extend it until final determination.

(d) If the Director finds that any licensee or applicant for licensing is no longer in existence or has ceased to do business as a broker-dealer, agent, or investment adviser, or is subject to an adjudication of mental incompetence or to the control of a committee, conservator, or guardian, or cannot be located after reasonable search, the Director may by order cancel the license or application for license.

(e) Withdrawal from licensing as a broker-dealer, agent, or an investment adviser becomes effective thirty days after receipt of an application to withdraw or within such shorter period of time as the Director may determine, unless a revocation or suspension proceeding is pending when the application is filed or a proceeding to revoke or suspend or to impose conditions upon the withdrawal is instituted within thirty days after the application is filed. If a proceeding is pending or instituted, withdrawal becomes effective at such time and upon such conditions as the Director by order determines. If no proceeding is pending on instituted and withdrawal automatically becomes effective, the Director may nevertheless institute a revocation or suspension proceeding under section 204(a)(2)(B) within one year after withdrawal became effective and enter a revocation or suspension order as of the last date on which licensing was effective.

(f) No order may be entered under any part of this section except the first sentence of subsection (c) without (1) appropriate prior notice to the applicant or licensee (as well as the employer or prospective employer if the applicant or licensee is an agent), (2) opportunity for hearing, and (3) written findings of fact and conclusions of law.

PART III—GENERAL PROVISIONS

SEC. 301. DEFINITIONS.—When used in these regulations, unless the context otherwise requires:

"Agent" means any individual other than a broker-dealer who represents a broker-dealer or issuer (except as provided in section 302) in effecting or attempting to effect purchases or sales of securities. A partner, officer, or director of a broker-dealer or issuer, or a person occupying a similar status or performing similar functions, is an agent only if he otherwise comes within this definition.

"Broker-dealer" means any person engaged in the business of effecting transactions in securities for the account of others or for his own account. "Broker-dealer" does not include (1) an agent, (2) an issuer, (3) a bank, savings institution, or trust company, or (4) a person who has no place of business in the District if (A) he effects transactions in the District exclusively with or through (i) the issuers of securities involved in the transactions, (ii) other broker-dealers, or (iii) banks, savings institutions, trust companies, insurance companies, investment companies as defined in the Investment Company Act of 1940, pension or profit-sharing trusts, or other financial institutions or institutional buyers, whether acting for themselves or as trustees, or (B) during any period of twelve consecutive months he does not direct more than fifteen offers to sell or buy into the District in any manner to persons other than those specified in clause (A), whether or not the offeror or any of the offerees is then present in the District.

"Commissioners" means the Commissioners of the District of Columbia, or their designated agent.

"Director" means the Director, Department of Licenses and Inspections of the District of Columbia, or his designated agent.

"District" means the District of Columbia.

"Fraud", "deceit", and "defraud" are not limited to common-law deceit.

"Guaranteed" means guaranteed as to payment of principal, interest, or dividends.

"Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as a part of a regular business, issues or promulgates analyses or reports concerning securities. "Investment adviser" does not include (1) a bank, savings institution, or trust company; (2) a lawyer, accountant, engineer, or teacher whose performance of these services is solely incidental to the practice of his profession; (3) a broker-dealer whose performance of these services is solely incidental to the conduct of his business as a broker-dealer and who receives no special compensation for them; (4) a publisher of any bona fide newspaper, news magazine, or business or financial publication of general, regular, and paid circulation; (5) a person whose advice, analyses, or reports relate only to securities exempted by section 302(a)(I); (6) a person who has no place of business in the District if (A) his only clients in the District are other investment advisers, broker-dealers, banks, savings institutions, trust companies, insurance companies, investment companies as defined in the Investment Company Act of 1940, pension or profit-sharing trusts, or other financial institutions or institutional buyers, whether acting for themselves or as trustees, or (B) during any period of twelve consecutive months he does not direct business communications into the District in any manner to more than five clients other than those specified in clause (A), whether or not he or any of the persons to whom the communications are directed is then present in the District; or (7) such other persons as the Director shall find are not within the intent of this paragraph.

"Issuer" means any person who issues or proposes to issue any security, except that (1) with respect to certificates of deposit, voting trust certificates, or collateral trust certificates, or with respect to certificates of interest or shares in an unincorporated investment trust not having a board of directors or persons performing similar functions or of the fixed, restricted management, or unit type, the term "issuer" means the person or persons performing the acts and assuming the duties of depositor or manager pursuant to the provisions of the trust or other agreement or instrument under which the security is issued; and (2) with respect to certificates of interest or participation in oil, gas, or mining titles or leases or in payments out of production under such titles or leases, there is not considered to be any "issuer".

"Net capital" means * * *.

(To be supplied if necessary.)

"Person" means an individual, a corporation, a partnership, an association, a joint stock company, a trust where the interests of the beneficiaries are evidenced by a security, an unincorporated organization, a government, or a political subdivision of a government.

"Sale" or "sell" includes every contract of sale of, contract to sell, or disposition of, a security or interest in a security for value; and "offer" or "offer to sell" includes every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security for value. Any security given or delivered with, or as a bonus on account of, any purchase of securities or any other thing is considered to constitute part of the subject of the purchase and to have been offered and sold for value. A purported gift of assessable stock is considered to involve an offer and sale. Every sale or offer of a warrant or right to purchase or subscribe to another security of the same or another issuer, as well as every sale or offer of a security which gives the holder a present or future right or privilege to convert into another security of the same or another issuer, is considered to include an offer of the other security. The terms herein defined do not include (A) any bona fide pledge or loan; (B) any stock dividend, whether the corporation distributing the dividend is the issuer of the stock or not, if nothing of value is given by stockholders for the dividend other then the surrender of a right to a cash or property dividend when each stockholder may elect to take the dividend in cash or property or in stock; (C) any act incident to a class vote by stockholders, pursuant to the certificate of incorporation or the applicable corporation statute, on a merger, consolidation, reclassifica-

tion of securities, or sale of corporate assets in consideration of the issuance of securities of another corporation; or (D) any act incident to a judicially approved reorganization in which a security is issued in exchange for one or more outstanding securities, claims, or property interests, or partly in such exchange and partly for cash.

"Securities Act of 1933", "Securities Exchange Act of 1934", "Public Utility Holding Company Act of 1935", and "Investment Company Act of 1940" mean the Federal statutes of those names as amended before or after the effective date of these regulations.

"Security" means any note; stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest or participation in any profit-sharing agreement; collateral-trust certificate; preorganization certificate or subscription; transferable share; investment contract; voting-trust certificate; certificate of deposit for a security; certificate of interest or participation in an oil, gas, or mining title or lease or in payments out of production under such a title or lease; or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for guarantee of, or warrant or right to subscibe to or purchase, any of the foregoing. "Security" does not include any insurance or endowment policy or annuity contract under which an insurance company promises to pay [a fixed sum of] money either in a lump sum or periodically for life or for some other specified period.

"State" means any State or possession of the United States, and Puerto Rico.

SEC. 302. EXEMPTIONS.—(a) Agents or issuers with respect to the following securities are exempted from sections 301(b) and 303:

(1) Any security (including a revenue obligation) issued or guaranteed by the United States, any State, any political subdivision of a State, or any agency or corporate or other instrumentality of one or more of the foregoing; or any certificate of deposit for any of the foregoing;

(2) Any security issued or guaranteed by Canada, any Canadian province, any political subdivision of any such province, any agency or corporate or other instrumentality of one or more of the foregoing, or any other foreign government with which the United States currently maintains diplomatic relations, if the security is recognized as a valid obligation by the issuer or guarantor;

(3) Any security issued by and representing an interest in or a debt of, or guarantees by, any bank organized under the laws of the United States, or any bank, savings institution, or trust company organized and supervised under the laws of any State;

(4) Any commercial paper which arises out of a current transaction or the proceeds of which have been or are to be used for current transactions, and which evidences an obligation to pay cash within nine months of the date of issuance, exclusive of days of grace, or any renewal of such paper which is likewise limited, or any guarantee of such paper or of any such renewal;

(5) Any investment contract issued in connection with an employees' stock purchase, savings, pension, profit-sharing, or similar benefit plan if the Director is notified in writing thirty days before the inception of the plan or, with respect to plans which are in effect on the effective date of these regulations, within sixty days thereafter (or within thirty days before they are reopened if they are closed on the effective date of these regulations).

(b) Agents or issuers with respect to the following transactions are exempted from the definition of "agent" in section 301, and from section 303:

(1) Any transaction between the issuer or other person on whose behalf the offer is made and an underwriter, or among underwriters;

(2) Any transaction in a bond or other evidence of indebtedness secured by real or chattel mortgage or deed of trust, or by an agreement for the sale of real estate or chattels, if the entire mortgage, deed or trust, or agreement, together with all the bonds or other evidences of indebtedness secured thereby, is offered and sold as a unit;

(3) Any transaction by a receiver or trustee in bankruptcy;

(4) Any offer or sale to a bank, savings institution, trust company, insurance company, investment company as defined in the Investment Company Act of 1940, pension or profit-sharing trust, or other financial institution or institutional buyer, or to a broker-dealer, whether the purchaser is acting for itself or in some fiduciary capacity;

(5) Any transaction pursuant to an offer directed by the offeror to not more than ten persons (other than those designated in paragraph (4)) in the District during any period of twelve consecutive months, whether or not the offeror or any of the offerees is then present in the District, if (A) the seller reasonably believes that all the buyers in the District (other than those designated in paragraph (4)) are purchasing for investment, and (B) no commission or other remuneration is paid or given directly or indirectly for soliciting any prospective buyer in the District (other than those designated in paragraph (4)); but the Director is authorized, as to any security or transaction or any type of security or transaction, for good cause, to withdraw or further condition this exemption, or increase or decrease the number of offerees permitted, or waive the conditions in Clauses (A) and (B) with or without the substitution of a limitation on remuneration:

(6) Any offer or sale of a preorganization certificate or subscription if (A) no commission or other remuneration is paid or given directly or indirectly for soliciting any prospective subscriber, (B) the number of subscribers does not exceed ten, and (C) no payment is made by any subscriber;

(7) Any transaction pursuant to an offer to existing securityholders of the issuer, including persons who at the time of the transaction are holders of convertible securities, nontransferable warrants, or transferable exercisable within not more than ninety days of their issuance, if (A) no commission or other remuneration (other than a standby commission) is paid or given directly or indirectly for soliciting any securityholder in this state, or (B) the issuer first files a notice specifying the terms of the offer and the Director does not by order disallow the exemption within the next five full business days;

(8) Any offer (but not a sale) of a security for which registration statements have been filed under the Securities Act of 1933 if no stop order or refusal order is in effect and no public proceeding or examination looking toward such an order is pending under such Act;

(9) Any transaction effected with existing employees, partners, or directors of the issuer if no commission or other remuneration is paid or given directly or indirectly for soliciting any person in the District.

(c) In any proceeding under these regulations, the burden of proving an exemption is upon the person claiming it.

SEC. 303. FILING OF SALES LITERATURE.—The Director is authorized to require the filing of any prospectus, pamphlet, circular, form letter, advertisement, or other sales literature or advertising communication addressed or intended for distribution to prospective investors, including clients or prospective clients of an investment adviser unless the security or transaction is exempted by section 302.

SEC. 304. MISLEADING FILINGS.—It shall be unlawful for any person to make or cause to be made, in any document filed with the Director or in any proceedings under these regulations, any statement which is at the time and in the light of circumstances under which it is made, false or misleading in any material respect.

SEC. 305. UNLAWFUL REPRESENTATIONS CONCERNING LICENSING OR EXEMPTION.—(a) Neither (1) the fact that an application for licensing has been filed nor (2) the fact that a person is effectively licensed constitutes a finding by the Director that any document filed under these regulations is true, complete, and not misleading. Neither any such fact nor the fact that an exception is available means that the Director has passed in any way upon the merits or qualifications of, or recommended or given approval to, any person, security, or transaction.

(b) It shall be unlawful to make, or cause to be made, to any prospective purchaser, customer, or client any representation inconsistent with subsection (a).

SEC. 306. ADMINISTRATION OF REGULATIONS.—(a) These regulations shall be administered by the Director, Department of Licenses and Inspections.

(b) It shall be unlawful for the Director or any of his officers or employees to use for personal benefit any information which is filed with or obtained by the Director and which is not made public. No provision of these regulations authorizes the Director or any of his officers or employees to disclose any such information except among themselves or when necessary or appropriate in a proceeding or investigation under these regulations. No provision of these regulations either creates or derogates from any privilege which exists at common

law or otherwise when documentary or other evidence is sought under a subpoena directed to the Director or any of his officers or employees.

[c. Insert a provision, if desired, covering fees for examinations, filings under section 303, and other miscellaneous filings for which no fees are specified elsewhere in these regulations.]

SEC. 307. INVESTIGATIONS AND SUBPENAS.—(a) The Director is authorized (1) to make such public or private investigations within or outside the District as he deems necessary to determine whether any person has violated or is about to violate any provision of these regulations, or to aid in the enforcement of these regulations, (2) to require or permit any person to file a statement in writing, under oath or otherwise as the Director determines, as to all the facts and circumstances concerning the matter to be investigated, and (3) to publish information concerning any violation of these regulations.

(b) For the purpose of any investigation or proceeding under these regulations, the Director or any officer or employee designated by him may administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda, agreements or other documents or records which the Director deems relevant or material to the inquiry.

(c) In the case of contumacy by, or refusal to obey a subpoena issued to, any person, the United States District Court for the District of Columbia, upon application by the Director, may issue to the person an order requiring him to appear before the Director or the officer designated by him, there to produce documentary evidence if so ordered or to give evidence touching the matter under investigation or in question. Failure to obey the order of the court may be punished by the court as a contempt of court.

(d) No person is excused from attending and testifying or from producing any document or record before the Director, or in obedience to the subpoena of the Director or any officer designated by him, or in any proceeding instituted by the Director, on the ground that the testimony or evidence (documentary or otherwise) required of him may tend to incriminate him or subject him to a penalty or forfeiture; but no individual may be prosecuted or subjected to any penalty or forfeiture for or on account of any transaction, matter, or thing concerning which he is compelled, after claiming his privilege against incrimination to testify or produce evidence (documentary or otherwise), except that the individual testifying is not exempt from prosecution and punishment for perjury or contempt committed in testifying.

SEC. 308. INJUNCTIONS.—Whenever it appears to the Director that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of these regulations, he may initiate appropriate action to enjoin the acts or practices and to enforce the compliance with these regulations. Upon a proper showing, a permanent or temporary injunction, restraining order, or writ of mandamus shall be granted and a receiver or conservator may be appointed for the defendant or the defendant's assets. The court may not require the Director to post a bond.

SEC. 309. CRIMINAL PENALTIES.—(a) Any person who willfully violates any provision of these regulations except section 304, or who willfully violates any order issued under the authority of these regulations, or who willfully violates section 304 knowing the statement made to be false or misleading in any material respect, shall upon conviction be fined not more than $300 or imprisoned for not more than ninety days; but no person may be imprisoned for the violation of any rule or order if he proves that he had no knowledge of the rule or order.

(b) The Director may refer such evidence as is available concerning violations of these regulations or of any order issued hereunder to the Corporation Counsel, who may, with or without such a reference, institute the appropriate criminal proceedings under these regulations.

(c) Nothing in these regulations shall limit the power of the United States or the District to punish any person for any conduct which constitutes a crime by statute or the common law.

SEC. 310. CIVIL LIABILITIES.—(a) Any person who—

(1) offers or sells a security in violation of section 201(a) or 305(b); or

(2) offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under

which they are made, not misleading (the buyer not knowing of the untruth or omission), and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission.

is liable to the person buying the security from him, who may sue either at law or in equity to recover the consideration paid for the security, together with interest at six percent per year from the date of payment, costs, and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he no longer owns the security.

(b) Every person who directly or indirectly controls a seller liable under subsection (a), every partner, officer, or director or such a seller, every person occupying a similar status or performing similar functions, every employee of such a seller who materially aids in the sale, and every broker-dealer or agent who materially aids in the sale are also liable jointly and severally with and to the same extent as the seller, unless the non-seller who is so liable sustains the burden of proof that he did not know and in exercise of reasonable care could not have known of the existence of the fact by reason of which the liability is alleged to exist. There is contribution as in cases of contract among the several persons so liable.

(c) Any tender specified in this section may be made at any time before entry of judgment.

(d) Every cause of action under these regulations survives the death of any person who might have been a plaintiff or defendant.

(e) No person may sue under this section more than two years after the contract of sale. No person may sue under this section (1) if the buyer received a written offer, before suit and for a time when he owned the security, to refund the consideration paid together with interest at six percent per year from the date of payment, less the amount of any income received on the security, and he failed to accept the offer within thirty days of its receipt, or (2) if the buyer received such an offer before suit and at a time when he did not own the security, unless he rejected the offer in writing within thirty days of its receipt.

(f) No person who had made or engaged in the performance of any contract in violation of these regulations, or who has acquired any purported right under any such contract with knowledge of the facts by reason of which its making or performance was in violation, may base any suit on the contract.

(g) Any condition, stipulation, or provision binding any person acquiring any security to waive compliance of any provision of these regulations is void.

(h) The rights and remedies provided by these regulations are in addition to any other rights or remedies that may exist at law or in equity, but these regulations do not create any cause of action not specified in this section or section 202(e).

SEC. 311. REVIEW OF ORDERS.—(a) Any person aggrieved by a final order of the Director may obtain a review of the order by the Board of Appeals and Review of the District of Columbia by filing, within fifteen days after the entry of the order, a written petition praying that the order be modified or set aside in whole or in part. A copy of the petition shall be forthwith served upon the Director, and thereupon the Director shall certify and file with the Board a copy of the filing and evidence upon which the order was entered. When these have been filed, the Board shall have jurisdiction to affirm, modify, enforce, or set aside the order, in whole or in part, and any such action by the Board shall be final. The findings of the Director as to the facts, if supported by competent, material and substantial evidence, shall be conclusive. If either party applies to the Board for leave to adduce additional material evidence, and shows to the satisfaction of the Board that there were reasonable grounds for failure to adduce the evidence in the hearing before the Director, the Board may order the additional evidence to be taken before the Director and to be adduced upon the hearing in such manner and upon such conditions as the Board may consider proper. The Director may modify his findings and order by reason of the additional evidence and shall file with the Board the additional evidence together with any modified or new findings or order.

(b) The commencement of proceedings under subsection (a) does not, unless specifically ordered by the Board, operate as a stay of the Director's order.

SEC. 312. FORMS, ORDERS AND HEARINGS.—(a) The Director may from time to time prescribe such forms and make such orders as are necessary to carry out the provisions of these regulations, including forms governing applications for

license and reports. For the purpose of forms, the Director may classify securities, persons, and matters within his jurisdiction, and prescribe different requirements for different classes.

(b) No form shall be prescribed, and no order shall be issued, amended or rescinded, unless the Director finds that the action is necessary or appropriate in the public interest or for the protection of investors and consistent with the purposes fairly intended by the policy and provisions of these regulations. In prescribing forms, the Director may cooperate with the securities administrators of the States and with the Securities and Exchange Commission with a view to effectuating the policy of these regulations to achieve maximum uniformity in the form and content of reports and applications for licenses wherever practicable.

(c) The Director is authorized to prescribe (1) the form and content of financial statements required by these regulations, (2) the circumstances under which consolidated financial statements shall be filed, and (3) whether any required financial statements shall be certified by independent or certified public accountants. All financial statements shall be prepared in accordance with generally accepted accounting practices.

(d) All forms prescribed by the Director shall be published.

(e) No provision of these regulations imposing any liability applies to any act done or omitted in good faith in conformity with any form or order of the Director, notwithstanding that the form or order may later be amended or rescinded or be determined by judicial or other authority to be invalid for any reason.

(f) Every hearing conducted under the authority of these regulations shall be public unless the Director in his discretion grants a request joined in by all the respondents that the hearing be conducted privately.

SEC. 313. ADMINISTRATIVE FILES AND OPINIONS.—(a) A document is filed when it is received by the Director.

(b) The Director shall keep a register of all applications for license which are or have ever been effective under these regulations and all denial, suspension, or revocation orders which have been entered under these regulations. The register shall be open for public inspection.

(c) The information contained in or filed with any application or report may be made available to the public in accordance with the provisions of these regulations.

(d) Upon request and upon such payment as the Director shall find will compensate the District for the cost of furnishing such service, the Director shall furnish to any person photostatic or other copies (certified under the seal of the District if requested) of any entry in the register or any document which is a matter of public record. In any proceeding under these regulations, or prosecution for violation of these regulations, any copy so certified is prima facie evidence of the contents of the entry or document certified.

(e) The Director shall refer to the Corporation Counsel for appropriate action requests from interested persons for interpretative opinions.

SEC. 314. SCOPE OF THESE REGULATIONS AND SERVICE OF PROCESS.—(a) Sections 101, 201(a), 305, and 310 apply to persons who sell or offer to sell when (1) an offer to sell is made in the District, or (2) an offer to buy is made and accepted in the District.

(b) Sections 101, 201(a), and 305 apply to persons who buy or offer to buy when (1) an offer to buy is made in the District, or (2) an offer to sell is made and accepted in the District.

(c) For the purpose of this section, an offer to sell or to buy is made in the District, whether or not either party is then present in the District, when the offer (1) originates from the District or (2) is directed by the offer or to the District and received at the place to which it is directed (or at any post office in the District in the case of a mailed offer).

(d) For the purpose of this section, an offer to buy or to sell is accepted in the District when acceptance (1) is communicated to the offeror in the District and (2) has not previously been communicated to the officer, orally or in writing, outside the District; and acceptance is communicated to the offeror in the District, whether or not either party is then present in the District, when the offeree directs it to the offeror in the District reasonably believing that the offeror is in the District and it is received at the place to which it is directed (or at any post office in the District in the case of a mailed acceptance.)

(e) An offer to sell or to buy is not made in the District when (1) the publisher circulates or there is circulated on his behalf in the District any bona fide newspaper or other publication of general, regular, and paid circulation which is not published in the District, or which is published in the District but has had more than two-thirds of its circulation outside of the District during the past twelve months, or (2) a radio or television program originating outside the District is received in the District.

(f) Sections 102 and 201(c), as well as section 305 so far as investment advisers are concerned, apply when any act instrumental in effecting prohibited conduct is done in the District, whether or not either party is then present in the District.

(g) Every applicant for licensing under these regulations and every issuer who proposes to offer a security in the District through any person acting on an agency basis in the common-law sense shall file with the Director, in such form as he may prescribe, an irrevocable consent appointing the Commissioners to be his attorney to receive service of any lawful process in any noncriminal suit, action, or proceeding against him or his successor executor or administrator which arises under these regulations or any order hereunder after the consent has been filed, with the same force and validity as if served personally on the person filing the consent. A person who has filed such a consent in connection with a previous licensing need not file another. Service may be made by leaving a copy of the process in the office of the Secretary of the Commissioners, but it is not effective unless (1) the plaintiff, who may be the Director in a suit, action, or proceeding instituted by him, forthwith sends notice of the service and a copy of the process by certified mail to the defendant or respondent at his last address on file with the Director, and (2) the plaintiff's affidavit of compliance with this subsection is filed in the case on or before the return day of the process, if any, or within such further time as the court allows.

(h) When any person, including any nonresident of the District, engages in conduct prohibited or made actionable by these regulations or any order issued hereunder, and he has not filed a consent to service of process under subsection (g) and personal jurisdiction over him cannot otherwise be obtained in the District, that conduct shall be considered equivalent to his appointment of the Commissioners to be his attorney to receive service of any lawful process in any noncriminal suit, action, or proceeding against him or his successor executor or administrator which grows out of that conduct and which is brought under these regulations or any order issued hereunder, with the same force and validity as if served on him personally. Service may be made by leaving a copy of the process in the office of the Secretary of the Commissioners, and it is not effective unless (1) the plaintiff, who may be the Director in a suit, action, or proceeding instituted by him, forthwith sends notice of the service and a copy of the process by registered mail to the defendant or respondent at his last known address or takes other steps which are reasonably calculated to give actual notice, and (2) the plaintiff's affidavit of compliance with this subsection is filed in the case on or before the return day of the process, if any, or within such further time as the court allows.

(i) When process is served under this section, the court, or the Director in a proceeding before him, shall order such continuance as may be necessary to afford the defendant or respondent reasonable opportunity to defend.

SEC. 315. CONSTRUCTION OF REGULATIONS.—These regulations shall be so construed as to effectuate the general purpose of making uniform the law governing persons dealing in securities and to coordinate the interpretation and administration of these regulations with the related Federal regulation.

SEC. 316. SHORT TITLE.—These regulations may be cited as the District of Columbia Uniform Securities Regulations.

SEC. 317. SEVERABILITY OF PROVISIONS.—If any provision of these regulations or the application thereof to any person or circumstance is held invalid, the invalidity shall not affect other provisions of applications of these regulations, and to this end the provisions of these regulations are severable.

SEC. 318. REPEAL AND SAVING PROVISIONS.

(See material on p. 148; U.L.A. 9C.)

SEC. 319. TIME OF TAKING EFFECT.—These regulations shall take effect on , 1962.

Mr. KORMAN. The Licensing Department does not feel that they are in a position to handle this type of licensing and supervision.

It requires much more expertise than they have in their organization. They think it requires a separate division of the other department or a separate department headed by an individual that might be akin to our Superintendent of Insurance.

It has been stated here this morning in connection with the recommendation that the District could take this over, Mr. Cary said, that the District authorities could act much more rapidly than they could.

I assumed from what he said that he believed we could step in and take away a license without the requirements of due process that the Securities and Exchange Commission now affords to holders of their registrations.

I hope that was not his recommendation because we have no more authority to step in and take away a license than the Securities and Exchange Commission has to take away a registration, and we would have to afford to the holder the same due process that they do.

It would take some time. It may be that under a "blue sky" law in some of the States the director has the right to summarily suspend operations during the investigation. But I would think the requirements of due process, certainly as practiced under the Federal jurisdiction of the District of Columbia, would require full hearing with charges and opportunity to be heard, counsel and so on, and the right of appeal, and in providing this we could not act with much more speed than the Securities and Exchange Commission could if they were empowered to do so.

Mr. MACK. Is this draft for the District government to adapt?

Mr. KORMAN. No, sir. This was a draft of the Uniform Securities Act, which was adapted to the District of Columbia for discussion purposes.

It is not in any final form at all, and was simply something to put before this group to discuss, to see whether we needed all of the items that were in there, or whether some should be changed, and so on.

This was the sole purpose of it. This is not a proposal for legislation at this point.

You will note, Mr. Chairman, that it does not encompass those parts of the uniform law which have to do with the registration of securities. It only has to do with those portions of it that have to do with the licensing or registration of dealers, agents, and advisers.

Mr. MACK. Does the District of Columbia have authority today to adopt these regulations?

Mr. KORMAN. No, sir.

Mr. MACK. In other words, you would require additional legislation, enabling legislation, before you could proceed?

Mr. KORMAN. That is right, sir.

Mr. MACK. This is not a rough draft of the legislation?

Mr. KORMAN. It is not, sir. It was merely compiled for discussion purposes. I wanted to tell you what we have done thus far. We have not as yet reported to the Commissioners.

I may say, sir, what I am saying here, is not necessarily their points of view. It is solely that of the Office of the Corporation Counsel, which is in the midst of its study.

Mr. MACK. Do you think we can solve our problem by amending section 15 of the Securities and Exchange Act, and by adopting legislation similar to this proposal, or this draft?

I refer to the discussion draft. In that way, we would be closing the gate at both ends of the field.

Mr. KORMAN. I gather, Mr. Chairman, from what Mr. Cary said—indeed, on page 17 of his statement, I find this:

> Under present law we could undoubtedly issue particular rules with respect to the District under the Securities Act of 1933.

I think they have, at present, fair authority.

I think if you amended section 15 of the 1934 act, as you have indicated, that that would give them sufficient authority to act completely in the District of Columbia.

Mr. MACK. Mr. Cary, under questioning, indicated he would need additional authority.

Mr. KORMAN. I am not quarreling with them. I have not studied their act sufficiently to say that he does or does not. I am merely going by what he says in his statement.

I gathered from what he said and from what was said in the discussions that we had at the office, that they almost have sufficient authority now and possibly with a little bit of authority from the Congress would be able to take care of the situation locally.

With all the expertise that they have there in the Department, with the fact that we do not presently think that it is necessary that the District should have a complete "blue sky" law in that we do not think we need to actually register new issues, the only thing they would be doing would be with the help of the National Association of Securities Dealers, policing the industry to the extent of policing the people who deal with it, and who advise others.

It is my personal point of view, and I limit it to my personal point of view, that it would be better for them, with all the facilities they now have, to take this over rather than the District of Columbia to take it over.

But I have not discussed that with the Commissioners of the District. We do believe that what has been disclosed indicates that some regulation is necessary.

Mr. MACK. I think it is quite obvious that we need some additional regulation or legislation to deal with this problem. It is far from being satisfactory.

I think Miss Ottenberg has done a valuable service here in acquainting you gentlemen with the problem, and calling it to the attention of other people.

Obviously, it was a deplorable condition.

I would also be interested in knowing whether or not you gentlemen were aware of the problem as it has existed since 1959? I wonder whether or not the Commissioners were aware of this problem prior to the time the articles were written?

Mr. KORMAN. I cannot speak for all the Commissioners, sir; but I am inclined to believe that they were not, or they would have taken some action to direct us to do something about it.

Mr. MACK. Then, what action has been taken since that time?

Mr. KORMAN. The action that has been taken since that time was for us to call all these people together that I enumerated earlier and have discussions of it to see what our present authority is and what might be necessary, and where is the best place for that authority to be lodged.

As I said earlier, it is my view that the best place, because of the facilities they now have and the knowledge and expertise that they have in the area, that this should be lodged with the Securities and Exchange Commission.

Mr. MACK. I presume you will make or you have made such a recommendation to the Commissioners?

Mr. KORMAN. We will, sir. We have not as yet. We had our last discussion only last week, and others are anticipated with some of this group to see whether the limited authority the Commissioners have now could be at all effective to take care of some of these ills.

As I said, our discussion indicates that the most that the Commissioners could do now would be to require licenses of some of these people.

Mr. MACK. Are you making such a recommendation?

Mr. KORMAN. Will we make that to the Commissioners?

Mr. MACK. Yes.

Mr. KORMAN. I have not discussed that fully with the Corporation Counsel.

Mr. MACK. In other words, no recommendation has been made?

Mr. KORMAN. No recommendation has been made. I am inclined to think that what we could do at the moment would not be completely adequate to take care of the situation, and that legislation of some sort should be suggested.

Mr. MACK. Of course, if the Commissioners do not have sufficient authority today, they can get authority from the Congress, if Congress feels it appropriate.

Mr. KORMAN. Yes, sir.

Mr. MACK. They have not made such a request, and you are not recommending that they do make such a request?

Mr. KORMAN. I am inclined to say this, sir: If this committee does not feel that it should give to the Securities and Exchange Commission the authority to enter the District of Columbia field more actively, then our recommendation would be to the Commissioners that they seek authority to do these same things by the District of Columbia government, which they do not have now.

They do not have, for instance, the authority to require of these people the posting of bonds, to require financial responsibility before entering the business, and so on.

These things would have to come from legislation. As I say, we would have to set up a completely new department and hire experts in this field, who would probably come from the Securities and Exchange Commission.

Mr. MACK. Changing the subject slightly, could I ask you about your program for the police to screen out these people who want to go into the securities business?

Mr. KORMAN. The most we could do would be to require an application from each one that wanted to be licensed and have that application processed by our police department, which would screen their own files to see what, if anything, they could find on it.

Mr. MACK. In other words, if they had a police record, you would not grant them a license?

Mr. KORMAN. That would probably be one of the provisions.

Mr. MACK. If they did not have the police record, they would probably get the license?

Mr. KORMAN. Probably so; yes, sir. I will not say in all instances; they might have some other shortcomings.

For instance, if we required them to get recommendations from others or required them to show that they had experience and they were unable to get recommendations, or the recommendations did not show them to be people who were trustworthy, I think we might be able to put such a limitation on within our present authority.

Or if they were unable to show that they had experience in the field, we might be able to deny them a license. But if you had someone who had no experience and wanted to enter the business for the first time, we have no facility, for instance, without legislation, to give them an examination.

Mr. MACK. As I understand, you are now studying the problem and you are going to make some recommendations of some kind; is that correct?

Mr. KORMAN. That is right, Mr. Chairman.

Mr. MACK. You have been studying the problem since February?

Mr. KORMAN. I will not say we have been studying the problem since February. At some time, the date of which I do not have before me, subsequent to the appearance of these articles, the Commissioners sent the problem to us.

In that interim, our office has been doing a great many other things and we have had, I think, either three or four meetings with this group over a period of about a month and a half, I would say.

There have been, between meetings, anywhere from a week to 10 days to 2 weeks. We also sent this out to the interested parties to study before we held any of these meetings, or after having had one meeting.

Mr. MACK. I want to thank you for your testimony.

Personally, I favor an amendment to the Securities and Exchange Act, but I do get the impression that the District government has not been sufficiently interested in this problem.

Mr. KORMAN. I think they have been, since the matter was called to their attention. Yes, they have been, indeed.

Mr. MACK. I also have the impression that they are extremely reluctant in assuming the responsibility for solving this problem on the local level?

Mr. KORMAN. On the contrary, Mr. Chairman, where situations of this sort have been pointed out to the Commissioners in other areas, and the matter has been studied, the Commissioners have come forward and sought legislation from the Congress, or have taken action on their own to remedy conditions.

One of those areas was that involving the sale and financing of automobiles, which, incidentally, was also brought forcibly to the attention of the Commissioners by a series of articles by Miss Ottenberg.

We went to the Congress and got authority to act in that case, and came up with a complete set of regulations, which took considerable time to frame, with the help of people in the industry.

We think we have corrected a great many, if not all, of the difficulties and problems in that industry.

A similar situation arose in connection with the home improvement contract business. We took similar action in that and have issued regulations to cover the situation.

In those instances, however, we were able, we thought, to take care of it entirely by comparatively simple regulations which could be administered by our Superintendent of Licenses, and simply by the issuance of licenses with certain limited restrictions.

But the securities business is one which is not quite so easy to regulate as is the sale of automobiles, or the repair of houses. It requires a setting up, we think now, of a department with experts who are thoroughly familiar with the industry, rather than simply setting it into our Licensing Department where complaints of factual situations can be resolved without a great deal of expertise.

This presents a problem which is not quite as simple as those others are. But in any event, the District is not treading water on this. The Commissioners have issued the instructions to us to investigate, and that is what we are doing.

We try not to act precipitously, but to act only after careful study.

Mr. Kneipp has an observation. I would be happy to have him make it to you directly, Mr. Chairman.

Mr. MACK. We will be glad to hear from you.

Mr. KNEIPP. Thank you, Mr. Chairman. I am sorry the clerk is not here. I would like to offer for the record, if I may, copies of what Mr. Korman has just referred to, the two sets of regulations and the two laws that were enacted by the Congress.

Mr. MACK. We will accept those for our files.

Mr. KNEIPP. The purpose in offering those, Mr. Chairman, is to demonstrate to the committee how the District has proceeded in matters of this kind heretofore.

First, an effort is made to mark out the limits of the Commissioner authority. That is what is in process now in that draft of April 20 that was furnished the chairman.

Then, having determined what existing law offers the Commissioners in the way of the authority, it is the practice of the Commissioners to go to the Congress and seek supplementary legislation.

In the case of the Home Improvement Contractors, Public Law 86–715 was a relatively simple bill to draft and to process through the Congress.

But in the case of the sales finance legislation, Public Law 86–431, it was a very complicated law. The Commissioners had to be given considerable additional authority over and above what they possessed under existing law.

I think, as Mr. Korman has indicated, it is anticipated now that additional authority to flesh out what the Commissioners now have in the way of dealing with securities dealers would be a rather complicated act to draft.

But the District is in process—the Corporation's Counsel's Office is in process of reviewing what is necessary to the end that a determination can be made as to the kind of law that may be necessary to give the Commissioners adequate authority in the field.

Mr. MACK. When do you expect to make your recommendations?

Mr. KORMAN. Mr. Kneipp has been carrying the laboring oar in this field. I would like him to answer the question.

Mr. KNEIPP. Mr. Chairman, as you can see, that draft is, I believe, about 40 pages in length. The group that Mr. Korman mentioned earlier has been working on that. We have not gotten very far because the problems that do come up create some difficulty in their determination.

It is a little hard to point out just how long, or to say just how long, it is going to be before we come up with some recommendation.

It might be that rather than try to deal with the matter by an adaptation of the Uniform Securities Act, to work just under the Commissioners' existing authority, which would allow them to require a showing of experience and character, require fingerprinting, reports, and fees, and then seek legislation, simple legislation, authorizing the Commissioners to require a bond and minimum capital of persons entering this field.

And also authorizing the Commissioners to set up an administrative agency with authorization for funds.

Mr. MACK. I cannot see any objection to doing that.

Mr. KNEIPP. That would be relatively simple to do.

Mr. MACK. At the same time, if the Congress would come in on it, I cannot see any objection to some type of local activity on the part of the District of Columbia government; that is, a recommendation for legislation.

Mr. KNEIPP. We could, Mr. Chairman, come up with relatively simple recommendations, merely "fleshing" out the authority of the Commissioners in certain limited respects, but not anything so complicated and detailed as the Uniform Securities Act.

This is the policy decision that has to be made at this time. Should we do it simply as we have done, for example, in the case of the home improvement contractors and the sales finance organizations?

Mr. MACK. I got the impression from Mr. Korman that if the Congress acted in regard to section 15 of the SEC, the District government would make no recommendations at all.

Mr. KORMAN. I think that would take care of the situation, Mr. Chairman, and I see, frankly, no reason why there should be two sets of regulations.

I would like to have the expression of the Congress as to what their will is. If they think that the Securities and Exchange Commission can better handle it, it would be certainly not our policy to try to take an opposite position.

Mr. MACK. I would not want that to be implied, even if the amendment were approved. I would not want it implied that the Congress felt that the District government should not interest itself in this

matter because we have merely amended the Securities and Exchange Act.

Mr. KORMAN. I do not think they would divorce themselves of it. Unquestionably, they would not. But merely licensing is one thing; regulating is another.

The regulation of an industry as complex as this may require a complete "blue sky" law and the setting up of another deparment of the District government.

This, I would say, requires rather careful study. That is what we are giving to it now.

Mr. MACK. Thank you, gentlemen, for your testimony.

I feel that the District should be a shining example of high, ethical standards. That is with regard to the securities business as well as other businesses.

I know the Congress has a responsibility. I furthermore feel that the District government has a responsibility of looking into matters of this nature, to see how we can improve a situation here in the District of Columbia.

This is our Nation's Capital, and the capital of the world, you might say. It disturbs me when we permit such an operation as this in the Nation's Capital.

Mr. KORMAN. I may say this much: I do not like to use the words "in defense," because it sounds like we have been amiss in our approach to this. I think this should be said, however, that with the presence of the Securities and Exchange Commission here in the Nation's Capital, with our knowledge of their general supervision of this business, I think possibly there may have been an assumption, not necessarily on the part of the District Commissioners, but on the part of the people generally, that this subject was taken care of here.

Not until the situation was called to our attention comparatively recently was there a realization that something more needed to be done.

Mr. MACK. I did not mean to be critical of the inaction on the part of the District government. But at the same time we have the Secret Service here, the Federal Bureau of Investigation, the Park Police, the Capitol Police, and in addition to that, you decided or we decided to have the Metropolitan Police.

You have a similar problem here with regard to regulations.

As I have indicated, I slightly favor the expansion of Federal jurisdiction.

I want to be certain, first, that the Securities and Exchange Commission has been diligent, has discharged its responsibility.

Personally, I favor the amendment which would expand jurisdiction with regard to the Securities and Exchange Commission.

But I also feel that the District government ought to interest itself in this area, and that they ought to make some kind of recommendations to the Congress, if we are in need of additional legislation.

Mr. KORMAN. We shall not discontinue what we are doing now. We shall carry it on to conclusion as quickly as possible, Mr. Chairman.

Mr. MACK. Thank you very much.

That concludes our hearing on this subject.

The committee stands adjourned.
("Investors Beware," by Miriam Ottenberg, follows:)

INVESTORS BEWARE

(By Pulitzer Prize Winner Miriam Ottenberg, Star staff writer)

A series exploring the practices of questionable investment firms, published by the Washington Star

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

The series of articles entitled "Investors Beware" written by Miriam Ottenberg for the Washington Star describe a situation of which every investor in Washington, D.C., should be informed. Growth in the number of securities firms operating here on the fringe of established ethics and the law has been of great concern to the vast majority of firms in the securities business, the NASD, and the SEC. Increased enforcement activity by NASD and the SEC has been effective; however, this alone cannot provide the full measure of protection which is needed.

An informed investor is capable of exercising commonsense when approached by a stranger representing the securities business who promises great profits in a short period. Miss Ottenberg's articles contain basic facts which could prove invaluable to investors.

Also, an informed investing public is essential if Washington is to have the right kind of securities law, properly administered.

If we are to deal promptly and well with the problems created by marginal firms moving into this area and realize the standards for which both the NASD and the SEC are striving, it will be in the light of analyses such as the "Investors Beware" series.

These articles deserve careful reading.

WALLACE FULTON, *Executive Director.*

[From the Washington (D.C.) Star, Feb. 4, 1962]

INVESTORS BEWARE—ONE OF THREE DISTRICT OF COLUMBIA BROKERS FOUND TO BE UNSAFE

(By Miriam Ottenberg, Star staff writer)

More than 100 firms are dealing in stocks and bonds in Washington, but one-third of them couldn't operate in most of the States.

That means the chances are one in three that the unwary Washington investor may run into a broker-dealer who knows nothing about the business or who pays the rent with his customer's investment money or who applies high-pressure tactics to sell questionable stocks.

The present danger to Washington investors is emerging in investigations conducted by the Securities and Exchange Commission, the National Association of Securities Dealers and the better business bureaus.

The steadily-worsening situation here in the promotion and sale of low-priced, over-the-counter securities lay behind the SEC's recent decision to send a task force of investigators into Washington on a clean-up mission.

The National Association of Securities Dealers, self-policing organization in the securities field, reports that, in its regular examinations of more than 100 investment firms here, it has recently been taking action against one out of three firms.

The better business bureau hired an ex-FBI agent to investigate Washington securities firms. On the basis of his findings of shoddy and unethical practices, the bureau called on the SEC and the dealers' association to increase their investigative staffs and step up enforcement activities here.

The bureau cited "the promotional activities and business methods of some of these securities firms (that) have resulted in severe losses to the investing public in this area."

RELIABLE FIRMS CONCERNED

Established investment firms here are seriously concerned by the sudden increase in inexperienced, financially unstable firms as well as the out-of-town promoters flocking into Washington.

The many reliable firms welcomed the better business bureau investigation and have labored with the dealers' organization in its self-policing activities as they see the city's reputation for safe dealings in securities threatened.

They are aware of the increasing number of victims—the stock-buying customers—many of whom are investing for the first time. Nearly 800 customers were caught in the collapse of one firm last year and their experience has been duplicated on a smaller scale by the customers of other firms.

These newcomer firms have opened their doors with promotional fanfare, accepted money from their customers to buy stock and closed their doors. In some cases, they have protected their investors. But, in other cases, the customers have been seriously hurt.

A Star survey of more than 60 firms which have opened for business here since January 1960 showed that approximately one-third of them have already gone out of business or been put out of business by the SEC or the National Association of Securities Dealers.

In one recent week alone, two Washington firms were expelled by the dealers' group and three Washington firms were named in actions launched by the SEC.

Since the start of 1960, the SEC has obtained injunctions against 11 Washington firms and revoked the dealer registrations of 9 firms. The SEC regional office covers Pennsylvania, Maryland, Virginia, West Virginia, Delaware and the District but, in the past 2 years, half the SEC actions against broker-dealers throughout the region have been against Washington firms.

During the same period, the National Association of Securities Dealers district committee has filed formal complaints against 44 Washington firms, expelled 18, suspended 1 and fined 20. It has revoked the registrations of 19 salesmen and fined 2—a total of $4,000.

The closed doors, the injunctions, revocations and complaints do not happen overnight. Before a firm's inexperience, lack of operating capital or questionable activities leads to formal action, plenty of customers have had a chance to lose their savings.

Both the SEC and the dealers' association report that evidence of violation of rules designed to protect the investing public is worse here than anywhere else in their regions.

Both bodies are aware of the prime cause: Washington has no local law to safeguard investors against questionable or financially unfit dealers.

NO LOCAL CONTROL

Unlike most States, Washington has no local control over the dealers or the stocks they sell. It has no requirement that broker-dealers be experienced or trained before going into the business of handling other people's money. It has no local control over salesmen. It also has no requirement that broker-dealers have any money of their own before they go into business.

With more stringent regulations going on the books in many Eastern States, promoters have gotten out one step ahead of legal action and moved into Washington where they feel comparatively safe until the SEC or the dealers' association catches up with them.

Out-of-town firms with no stock exchange connections have opened branch offices here to escape the local controls exerted over their headquarters in other States.

Characteristic of some of the newcomer firms are their fancy names, many of which are so close to those of established firms as to be indistinguishable when said fast. The names also are designed to give the impression to customers that a two-room firm has nationwide connections.

The lack of operating capital, however, is rated particularly dangerous to the customers. Until the SEC pins down a violation of its rule that a firm cannot owe 20 times more than its net capital, some of these firms use their customers' money to pay the rent, promote their business and furnish their offices. When their doors close, the customers' money—if there's anything left—can be attached by other creditors.

The Star's survey of newcomer firms showed seven have gone into busines here in the past 2 years with $500 or less in cash. One of them started with $100. More than half started with less than $5,000. Many were in the hole financially with the costs of launching their business before they even began accepting customers' money to buy stocks.

Their lack of experience in the business is equally apparent—and as potentially harmful to the customers.

EXPERIENCE LACK SHOWN

Of the 45 firms who have registered with the SEC since the start of 1960 and are still in business, the Star's survey showed that 7 had no previous experience in the securities field. Four reported less than a year's experience. Nine got their own training as salesmen for a now defunct firm or in one of the firms stemming from it. In 10 firms, only 1 member of the company had any previous experience. In only 11 of the 45 firms, all the partners had some previous experience but frequently not much of it.

[From the Washington (D.C.) Star, Feb. 5, 1962]

INVESTORS BEWARE—VARIOUS TECHNIQUES USED TO LURE UNWARY

(By Miriam Ottenberg, Star staff writer)

The techniques for selling low-grade stocks to unwary Washington investors range from elaborate stage settings to fast telephone patter.

While the stock promoters pretend the greatest solicitude for the safety of their customers' money and act as though their only concern is to let a client in on a good thing, their actual goal is to make a killing before the stock they tout becomes worthless.

They can get away with their gimmicks here longer than in most other places because Washington has no law to assure local controls over the investment firms or their salesmen.

Washington has many reliable, firmly established investment firms but one-third of those in business here today would not be allowed to operate in most other cities.

EXAMPLES OF TECHNIQUES

Selling techniques of some stock promoters are shown in reports of an ex-FBI agent who "shopped" Washington investment firms for the Better Business Bureau, in customer complaints and in reports of unethical practices furnished by Washington's reputable firms. Here's the pattern:

1. To create the impression that stocks of little value are being heavily traded, the promoter installs a blackboard in his office and changes the stock quotations on it hourly.

While a customer listens, the promoter calls a well-known investment firm and asks for the latest price on a stock. When the promoter gets the answer, he tells the customer: "See, the big boys are trading in this, too."

JUST WINDOW DRESSING

The impressed customer doesn't realize that the blackboard quotations are just window dressing. He doesn't know that the answer given by the big firm was simply read from the daily sheet of over-the-counter listings and that a reputable firm wouldn't touch the particular stock. He also is unaware that the buying price of the stock given to him is substantially higher than the price the promoter got over the telephone.

Reputable firms are trying to curb this practice by offering to call back with the answer when they suspect a fly-by-night outfit is on the other end of the telephone. If their suspicions are proved correct, they don't call back—but they can't detect them all.

2. To create the illusion of respectability, a shoestring outfit claims it is trading regularly with one of the well-known firms.

To prove it, the promoter flashes a bill on the letterhead of the big investment house. The bill was easy to come by. The promoter simply ordered some well-known stocks or bonds as any customer could do. Even if he lost a little money on the deal, he has evidence to show the doubting customers that he does business with recognized firms.

3. To attract servicemen with a few dollars to invest, the promoters recruit officers retiring from the Armed Forces as salesmen or junior partners. The promoters are attracted by the service contacts of these former officers as well as by their savings.

The ex-FBI agent working with the better business bureau reported hearing a promoter addressing several telephone callers by their officer rank, and added: "It has become rather obvious during this investigation that the Armed Forces offer a tremendous market for over-the-counter dealers."

A number of the letters from customers who lost their savings in the collapse of one Washington firm came from both officers and enlisted men.

ATTRACTING SALESMEN

4. To attract salesmen with some money of their own, the promoters put help-wanted ads for salesmen in the newspapers on the same day they advertise spectacular new issues.

When the would-be salesmen apply for jobs, they have to agree to invest in these questionable new stocks themselves before they can go to work. They are expected to get their relatives and friends into the deal, too. To milk them a little more, the promoters make them pay various fees as well as a lump sum for so-called training.

The wife of one salesman who went into a now defunct firm complained that her husband had given up a good job in another field, invested all their savings in the stocks he was supposed to sell, and ended up with neither savings nor job.

VARIOUS GIMMICKS

5. To drain the financial resources of their customers the promoters have several gimmicks.

One convinced a customer to cash in his life insurance and put the money in low-priced stocks which would grow and grow in value.

The head of another firm here told the better business bureau investigator that customers left their money with him and authorized him to use his own discretion in buying and selling stocks. The reputable firms, with plenty of capital behind them, are extremely cautious about accepting any such discretionary accounts and do it only in individual cases for longstanding customers.

A similar promoter concentrates on older people who have clung through the years to a few "blue chip" stocks. They are advised to sell the "blue chips" because they can get more income out of a lower priced stock. They are not warned that a promised 8 percent dividend might be accompanied by a greater risk. So they give up safe investments in favor of stock in struggling young companies that can't make ends meet.

TELEPHONE USE

6. To promote sales, promoters hire a battery of part-time telephone salesmen. Prospective customers called at random are told a stock selling for $2 has just gone up an eighth and the "inside" word from New York is that it actually has gone up a quarter. No reputable firm would bother to use fractional changes to interest investors but the salesmen are trained to give the impression that the stock is moving fast and the time to get in on quick profits is now.

Or prospective investors are told the salesman has "inside information" about a contemplated merger, a spectacular earnings report, a new invention, an extra dividend, a big order the company has just received, or a successful test of a complicated gadget.

Some of the promoters have imported high-pressure salesmen from New York. One of their favorite gambits is the earnest assurance that the salesman has bought stock in this venture for his mother. Obviously, the customer is led to believe, if a man put his own mother's money in this stock, it must be safe.

ANOTHER ARGUMENT

Or the argument is advanced that low-priced stocks are safer to buy because they can't drop as far as the high-priced stocks.

Complaints from the public indicate that many of those fleeced were buying stocks for the first time. Typical of their innocence is one victim's remark that she did not investigate the salesman before she let him take her money because she thought all stock salesmen had to be licensed.

In many places, both the investment firms and their salesmen are subject to local regulation, but not in Washington.

[From the Washington (D.C.) Star, Feb. 6, 1962]

INVESTORS BEWARE—CASE OF 1 FIRM AND 800 VICTIMS

(By Miriam Ottenberg, Star staff writer)

When a Washington investment firm called American Diversified Securities, Inc., closed its doors last year close to 800 customers were caught in the collapse. Their claims amount to over half a million dollars.

Nobody is sure yet what can be salvaged for the customers and other creditors, but the company's ultimate deficit is expected to run over a million dollars.

The story of the rise and fall of American Diversified is the story of what can happen in a community without a local law to protect investors from inexperienced and undercapitalized investment firms.

OFFSHOOTS SPROUT UP

It is a continuing story, because many of American Diversified's former salesmen and associates have opened investment firms of their own—and some of them have already run afoul of Federal regulations.

Six have been named in proceedings by the Securities and Exchange Commission or the National Association of Securities Dealers. Four others have closed. At least seven are still in business. Among other newcomers to the burgeoning securities business here are broker-dealers who gained their only experience in firms launched by former American Diversified salesmen.

Some of these offshoots presumably have learned something from the experience of American Diversified and are trying to conduct a different kind of business. But a survey shows that others belong in the one-third of Washington investment firms which wouldn't be allowed to operate in most States.

Most of American Diversified's successors are selling the same kind of stock, using the same sales methods and operating with the same lack of experience and shaky financing that contributed to American Diversified's boom-and-bust history.

BEGAN AS ONE-MAN FIRM

American Diversified had its origin in a one-man company launched in February 1958, with $2,200 and no previous experience in the securities business. It incorporated in August 1958.

Its cash amounted to less than $3,000 when it launched its plan to raise the capital to keep going. It started issuing stock in its own newly formed corporation and announced its program to organize mutual funds among members of national organizations.

During 1959, according to a report of a court-appointed accountant, 49,000 shares of American Diversified stock were sold. Ultimately, this accountant reported, $335,000 was raised through stock sales. People paid as much as $28 a share for American Diversified stock.

The mutual fund concept which had attracted stockholders never got off the ground. While waiting for it to materialize, the company engaged in selling over-the-counter securities and started underwriting stock issues.

EXPANDED RAPIDLY

The company rapidly expanded. From 20 employees in 1958, it had grown to 120 by September 1960. Like similar companies, it took on retired officers from the Armed Forces who could and did interest officers and enlisted men in the low-priced stocks being offered by the company.

Among its other salesmen were former used-car salesmen, discount house salesmen, electricians, men's wear salesmen, floor managers, and hotel clerks. Much of their business was done by telephone.

American Diversified spread out. It opened a Philadelphia office, merged with another company and, in the fall of 1960, opened offices in Miami and New York.

At that point, the Securities and Exchange Commission moved in. The SEC tries to protect the investing public by requiring the firms entrusted with the public's money to keep a proper record showing who owes what to whom.

COURT ISSUES INJUNCTION

In September 1960, district court, at the request of the SEC, enjoined American Diversified from doing business until its books and records complied with SEC rules. A SEC investigator reported at the time that the books were 3 months behind and that the firm had about 3,000 customers' accounts "many of which contain inaccurate securities positions and errors which reflect purchases for which the firm has not received payment and many unrecorded receipts and deliveries of securities."

Summarizing American Diversified's rapid expansion and its first setback, the court-appointed accountant reported:

"Despite this feverish growth, the company at no time earned any income. * * * For the most part, the company was living on its expectations. The company had geared itself to a high-volume operation. When such was not forthcoming, losses became severe. The SEC shutdown for the fall of 1960 was a heavy burden to overcome. Opening two new offices during this same period was an excessive one."

PRESSES STOCK DRIVE

After the SEC shutdown, American Diversified brought in a national accounting firm to straighten out its books. The firm, according to a later report, had to make more than 1,000 corrections in the records.

When the records were adjusted, the company was allowed to reopen for business in January 1961.

In less than 2 months, it was in financial trouble because of its heavy operating expenses and vast corps of salesmen. The court-appointed accountant tells how the company, faced with a second shutdown, zeroed in on one stock and feverishly began promoting it. The chosen stock went from $7 a share on March 11 to 21⅞ by April 3.

American Diversified salesmen were busy. Letters from customers who were solicited to buy the chosen stock during the March drive are now in the files of the trustee in bankruptcy in the American Diversified case.

One midwestern customer said he was called long distance on March 20 and advised to buy 50 shares of the chosen stock at $13 a share. He said he was called again a week later by the same salesman, who told him the stock had been recommended by a New York investment house which sounded to him like Rothschild. Urging him to buy more, the salesman said the stock was now selling at $20 and was expected to go much higher.

BOUGHT $6,000 OF STOCK

A Washington doctor, also solicited by telephone, reported he bought $6,000 worth of the stock on March 17. A Washington woman wrote that she bought $237.50 worth of the stock on March 13 and added that "this may not appear to be an impressive transaction, but these shares were paid for out of savings accumulated through 11 years of hard work as a waitress."

A Shreveport, La., man isn't sure exactly what he bought. He knows he bought 50 shares of this stock on January 17 and sold 25 shares on March 13. Then, he said, he was notified the next day that he had sold another 25 shares but his salesman told him to ignore that notice because it was a mistake and he still had 25 shares. On March 27, he was notified that he had sold his remaining

25 shares but in April he was advised that he had bought 50 shares, "which was news to me."

COULDN'T PAY FOR SHARES

The flurry of activity reflected in these letters and dozens like them climaxed when American Diversified couldn't pay for the shares it had ordered from other brokers to fill its customers orders. It tried to cancel the orders but most of the brokers refused to allow cancellation and American Diversified was stuck. Customers clamored for payment on the stock they had sold or stock certificates for the shares they had bought. American Diversified had neither enough money nor stock to satisfy its customers.

At that point, the company was so far in the hole that it had clearly violated the SEC rules forbidding a securities dealer from owing 20 times more than his net capital. On April 6, a district court judge, at the request of the SEC, granted a temporary restraining order to halt American Diversified from transacting business until it could comply with the net capital rule.

An SEC affidavit filed in court at that time reported that the company's deficiency in capital amounted to $217,804.47 and aggregate indebtedness to all others amounted to $1,064,416.91. Among these others were the customers who had been pressed to buy the "hot" stock—which is now selling at around 50 cents.

VICTIMS ARE MANY

They weren't the only victims. The letters sent to the trustee in bankruptcy reflect the disappointment, despair and heartache of many others who never received the stock they bought nor were paid for the stock they sold.

One man wrote that he had put money into American Telephone & Telegraph stock over many years while he was saving to buy a home. When he thought he had enough, he turned over his 60 shares of A.T. & T. to American Diversified to sell for him. He should have gotten a check within 5 days. When it didn't come in 2 weeks, he asked questions and was told the check had been sent to the wrong address. He couldn't understand that because the confirmation of the sale had reached him all right. By the time the check finally arrived, the the company was in receivership and payment had been stopped.

A Florida mother said she went into the stock market early last year to make a quick profit to help finance her daughter's operation. When the time came to sell the stock and take her profit, she still hadn't received the stock certificates. So she couldn't sell. She is still waiting for $2,795 in stock certificates or cash.

CERTIFICATE STATUS UNCERTAIN

The stock certificates of some of the customers have been located, but it hasn't been decided yet whether they're entitled to the stock they bought or whether they must join the other customers in participating in whatever can be salvaged from the collapse.

Some of the stock certificates won't help the customers much now, in any case. If they had received the certificates when they were supposed to they could have sold at a profit or at least broken even. Now, several of the issues touted by American Diversified salesmen have fallen more sharply than they rose and today are only worth a fraction of what they cost.

Last June, after the court-appointed accountant went over the books of American Diversified and attempted to trace the transactions, he reported to the receiver:

"There are many peculiar, strange and mystifying transactions which have created a substantial feeling of uncertainty on our part. * * * We recommend further investigation."

HOW TO PICK A BROKER

There are many reliable, established investment firms in Washington with whom you can invest with confidence. To would-be investors, they give this advice:

1. Know the investment firm. Check with your banker or other financial adviser on the firm's background and reputation.

2. Insist on reading the prospectus or circular before you invest in a new stock to understand just how much risk is involved.

3. Never buy stocks on the basis of unsolicited telephone calls. This is the high-pressure approach that can lure you into losing money.

4. If a salesman makes extravagant promises about a new or recently issued stock but declines to put his statements in writing, watch out—and report to the Securities and Exchange Commission or the National Association of Securities Dealers.

[From the Washington (D.C.) Star, Feb. 7, 1962]

INVESTORS BEWARE—LAW IS NEEDED HERE TO PROTECT BUYERS

(By Miriam Ottenberg, Star staff writer)

Investors in 48 States are better protected against unscrupulous or financially unfit investment firms than are the investors in the Nation's Capital.

Everywhere in the country but Delaware, Nevada, and the District of Columbia, some form of "blue sky" law regulates securities dealers and the stocks they trade.

Most of these State laws would prevent one-third of Washington's investment firms from operating. That's the conservative estimate of the proportion of marginal firms here.

State enforcement of "blue sky" laws is part of a three-pronged defense against unqualified investment firms and questionable stocks. The other two prongs are the Securities and Exchange Commission and the National Association of Securities Dealers.

Washington lacks the first prong—a local law to keep out undercapitalized, underexperienced, and unethical firms peddling questionable stocks.

As a result, the other two prongs—the SEC and the dealers' association regional offices—report more complaints and more violations of securities rules here than anywhere else in their regions.

To cope with the local problem, the SEC has sent a task force of investigators into Washington on a cleanup drive. The National Association of Securities Dealers has stiffened its examination requirements for those selling stock, but the dealers' association's self-policing efforts cover only its own members. At least seven of the recently established firms here are not members.

Many of the States have recently tightened their securities laws. A number of them have amended their laws to conform to the tough Uniform Securities Act, a model State law drafted by a board of experts. These actions have prompted more out-of-towners to come to Washington where they can operate free from local controls.

Maryland has a "blue sky" law but proposes to tighten it. A committee appointed by Governor Tawes has come up with a draft of legislation closely paralleling the Uniform Securities Act. Governor Tawes has already tagged it as a priority measure for the new session of the Maryland General Assembly. If Maryland succeeds in tightening its law, some of its ousted promoters can be expected to cross the line into Washington.

Virginia has a strict law patterned after the uniform act. The Virginia law, regulations drafted under it and its forthright enforcement are widely regarded as successful in keeping questionable operators out of the State.

THREE CONTROLS

Generally, the State laws provide these three types of regulations:

1. Antifraud provisions which enable "blue sky" administrators to issue public warnings, investigate suspected fraud, move in fast to stop fraudulent activities and punish malefactors.

2. Registration or licensing of broker-dealers and their salesmen, which is aimed at keeping out the unqualified or unethical, assuring supervision of their activities and putting them out of business if they fall below required standards.

3. Registration of the securities to be sold in a State, which assures that the investors can learn about what they are buying and that stocks violating either State or Federal laws are not circulating.

PROTECTION SLIGHT

In Washington, a survey by the Star disclosed, customers have been hurt most by the lack of any requirement that investment firms must have any cash of their own to do business. The only protection offered to Washington investors is the SEC rule that forbids a securities firm from owing more than 20 times

its net capital. However, by the time investigators discover this rule has been violated, the firm often has used up the customer's money on rent and promotion. The firm's doors are shut, but that doesn't help the customer who got hurt.

The Star's survey showed that more than half the investment firms going into business here since January 1960, started with less than $5,000 and one only had $100.

Virginia authorizes its State corporation commission to require a $25,000-surety bond to protect investors. The proposed Maryland act requires the broker-dealer to maintain a net capital of at least $15,000 and makes him subject to posting a surety bond up to $10,000.

Among other States, Michigan can require the broker-dealer to show up to $100,000 in capital. New Hampshire sets the figure at $25,000, and Pennsylvania recently raised its required capital from $10,000 to $25,000.

TRAINING IS LACKING

In Washington, lack of experience has proved the downfall of some investment firms which traded themselves into bankruptcy and took their customers' money with them. No training or experience is required here of either the broker-dealers or their salesmen. If the firms stay out of the National Association of Securities Dealers, even the protection of an examination is lost.

The lack of experience was clearly revealed in the Star's survey of newcomer firms where some of them had no experience, some had less than a year and less than a third of them could report that all members of the firm were experienced.

In contrast, half the State laws refer to lack of training or inexperience as sufficient grounds to keep a broker-dealer out of business.

Virginia requires a broker-dealer to have 3 consecutive years of experience in the securities business before he can register. If the firm is a partnership, the majority of the firm's members must have 3 years' experience and if it's a corporation, at least two officers must meet the experience qualification.

Maryland's proposed law allows the commissioner administering the "blue sky" law to deny registration to a broker-dealer lacking training, experience or knowledge of the securities business. It also allows him to require an examination of both broker-dealers and salesmen.

SITUATION ON FRAUD

In Washington, no local law deals specifically with fraudulent practices in securities. The city is protected by Federal law more fully than the States since all but a few securities here are considered interstate and subject to SEC rules.

Virginia's law and Maryland's proposed law, however, offer the kind of broad cover that would give the U.S. attorney here some clear-cut law to use against fraud artists in the securities field if Washington had a local law.

Virginia's law, paralleled by the Maryland proposal, makes it unlawful to employ any device, scheme, or artifice to defraud in the offer or sale of any security, directly or indirectly. It also makes it a crime to obtain money or property by untruth or omission of a material fact or to engage in any practice which defrauds or could defraud or deceive the stock purchaser.

RULES ON CRIMINALS

In Washington, a man with a criminal record can go into the business of dealing with other people's money as long as his record doesn't involve securities. The SEC rules bar the registration of anyone convicted in the past 10 years of a crime involving securities or the conduct of the broker-dealer's business. The SEC also bars those previously enjoined in connection with securities transactions or cited by the SEC for violating its laws or regulations.

Virginia's law requires that the broker-dealer be of good character and reputation. Virginia's commission can revoke or refuse to renew a registration in the public interest or if the broker-dealer has engaged in a fraudulent transaction, become insolvent, faces insolvency, or has been convicted of a misdemeanor involving securities or any felony.

Maryland's proposed law allows the commissioner to deny or revoke a license for any felony conviction, any false or misleading statements on the registration, any dishonest or unethical practice in the securities business or insolvency.

FAST FRAUD ACTION

Virginia's law and Maryland's proposed law allow the administrator to move fast against the unethical or fraudulent stock dealer—faster than the authorities can move in Washington.

Both the SEC and the National Association of Securities Dealers acknowledge that they can rarely go after the unqualified, financially unfit, and unscrupulous firms in Washington until some customers have already been hurt.

"The reason they're selling junk stocks here," one securities official summed it up, "is because the people coming in are promoters. They don't have the capital or the experience to deal in good stocks even if they wanted to."

Experts in the field, from official investigators to reputable investment executives, are convinced the promoters will continue to prey on Washington investors as long as there's no local law on the books to discourage them.

AFTERMATH

Reaction to the foregoing series came swiftly. There were these developments:

The day after the last of the series appeared, a special committee of Washington investment dealers voted to recommend a local law to insure more protection for the city's investors. The committee was appointed by the Bond Club of Washington, whose 300 members represent a substantial segment of the city's investment community.

The following day, the executive director of the National Association of Securities Dealers and the regional director of the Securities & Exchange Commission covering the Washington area both publicly urged a local law to protect the public form unscrupulous or financially shaky investment firms.

The House Commerce Subcommittee chairman in charge of SEC legislation requested the SEC to comment on the accuracy of the series, and the adequacy of SEC regulation of the securities business in Washington.

The SEC promptly replied:

"We, of course, are familiar with Miss Ottenberg's articles. Indeed, she substantiated many of the facts by consultation with members of our staff. While we have not checked every detail, we are satisfied with the essential accuracy of her articles and we believe Miss Ottenberg has rendered a valuable public service.

"We have been aware for some time of a substantial increase in the questionable activities of a class of securities dealers in the Washington area, many of whom have been newcomers here."

The SEC went on to report that it had assigned a task force to Washington to step up its enforcement activities against the new crop of questionable dealers but warned that "this shifting of personnel does not meet the problem fully, is made at the expense of other responsibilities, and can only be temporary because the District of Columbia is by no means our only trouble spot."

Further confirmation of the problems pinpointed in the series came when the Star learned that a broker barred in New York had opened for business here. In the following days, in the SEC started proceedings to revoke his license and ordered proceedings to determine whether four other Washington investment firms and two New York Stock Exchange firms with Washington branch offices should be stopped from doing business.

As the demand for regulation became stronger, the president of the Board of District Commissioners, ordered the Corporation Counsel to draft rules to license dealers and their salesmen. The city's attorney promptly called a meeting of local and national experts in the field and found general agreement that new controls were needed to protect Washington investors.

The U.S. Attorney for the District of Columbia called on the authorities to provide him with existing complaints with an eye toward criminal prosecution. The SEC promptly turned over four cases.

As for the investors themselves, brokers reported that their customers, for the first time, were asking detailed questions about the securities being sold and the background and reputation of the investment firms with which they were doing business.

MIRIAM OTTENBERG

Author of "Investors Beware" she won the Pulitzer Prize for 1960 for her series exposing a used-car racket in the Nation's Capital.

She has delved into many phases of crime, communism, and corruption. She covered the Senate investigations of the dope traffic and campaigned for strengthened narcotics laws. She covered and interpreted the findings of the Kefauver committee in its exposé of crime syndicates and dug into the activities of the "Five Percenters."

Her investigations in the Nation's Capital have led to more law enforcement tools against violators as well as pioneering laws in the fields of mental illness, sexual psychopaths, narcotics addiction, and mandatory commitment of the criminally insane. Her exposés of unethical practices in the used-car and home-improvement fields have led to public awareness of consumer pitfalls as well as corrective legislation.

In an unprecedented tribute to a newspaper reporter, the law-enforcement community and civic leaders gave a reception in her honor, in 1958, where she was presented with a plaque signed by the Attorney General of the United States, congressional leaders, judges, prosecutors, and the chief of police.

(Whereupon, at 12:52 p.m., the hearing in the above-entitled matter was concluded.)

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