

FEDERAL SECURITIES EXCHANGE ACT OF 1934

APRIL 17 (calendar day, APRIL 20), 1934.—Ordered to be printed

Mr. FLETCHER, from the Committee on Banking and Currency,
submitted the following

REPORT

[To accompany S. 3420]

The Committee on Banking and Currency, to whom was referred the bill (S. 3420) to provide for the regulation of securities exchanges and of over-the-counter markets operating in interstate and foreign commerce and through the mails, to prevent inequitable and unfair practices on such exchanges and markets, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass. This bill is a substitute for the bill (S. 2693) introduced on February 9, 1934, and on which extensive hearings were held.

There follows a statement regarding the nature of the bill as reported, a general analysis thereof, and a summary of the bill by sections.

I. INTRODUCTORY STATEMENT

1. The President's Message

On February 9, 1934, the President sent the following message to Congress:

To the Congress:

In my message to you last March proposing legislation for Federal supervision of national traffic in investment securities I said, "This is but one step in our broad purpose of protecting investors and depositors. It should be followed by legislation relating to the better supervision of the purchase and sale of all property dealt with on exchanges."

This Congress has performed a useful service in regulating the investment business on the part of financial houses and in protecting the investing public in its acquisition of securities.

There remains the fact, however, that outside the field of legitimate investment, naked speculation has been made far too alluring and far too easy for those who could and for those who could not afford to gamble.

Such speculation has run the scale from the individual who has risked his pay envelop or his meager savings on a margin transaction involving stocks with whose true value he was wholly unfamiliar, to the pool of individuals or corpora-

tions with large resources, often not their own, which sought by manipulation to raise or depress market quotations far out of line with reason, all of this resulting in loss to the average investor, who is of necessity personally uninformed.

The exchanges in many parts of the country which deal in securities and commodities conduct, of course, a national business because their customers live in every part of the country. The managers of these exchanges have, it is true, often taken steps to correct certain obvious abuses. We must be certain that abuses are eliminated and to this end a broad policy of national regulation is required.

It is my belief that exchanges for dealing in securities and commodities are necessary and of definite value to our commercial and agricultural life. Nevertheless, it should be our national policy to restrict, as far as possible, the use of these exchanges for purely speculative operations.

I therefore recommend to the Congress the enactment of legislation providing for the regulation by the Federal Government of the operations of exchanges dealing in securities and commodities for the protection of investors, for the safeguarding of values, and so far as it may be possible, for the elimination of unnecessary, unwise, and destructive speculation.

FRANKLIN D. ROOSEVELT.

THE WHITE HOUSE, February 9, 1934.

The foregoing message was supplemented by a letter from the President to the Chairman of the Committee on Banking and Currency under date of March 26, 1934. The President's letter is as follows:

HON. DUNCAN U. FLETCHER,
Chairman Banking and Currency Committee,
United States Senate, Washington, D.C.

MY DEAR MR. CHAIRMAN: Before I leave Washington for a few days holiday, I want to write you about a matter which gives me some concern.

On February 9, 1934, I sent to the Congress a special message asking for Federal supervision of national traffic in securities.

It has come to my attention that a more definite and more highly organized drive is being made against effective legislation to this end than against any similar recommendation made by me during the past year. Letters and telegrams bearing all the earmarks of origin at some common source are pouring into the White House and the Congress.

The people of this country are, in overwhelming majority, fully aware of the fact that unregulated speculation in securities and in commodities was one of the most important contributing factors in the artificial and unwarranted "boom" which had so much to do with the terrible conditions of the years following 1929.

I have been definitely committed to definite regulation of exchanges which deal in securities and commodities. In my message I stated, "It should be our national policy to restrict, as far as possible, the use of these exchanges for purely speculative operations."

I am certain that the country as a whole will not be satisfied with legislation unless such legislation has teeth in it. The two principal objectives are, as I see it—

First, the requirement of what is known as "margins" so high that speculation, even as it exists today, will of necessity be drastically curtailed; and

Second, that the Government be given such definite powers of supervision over exchanges that the Government itself will be able to correct abuses which may arise in the future.

We must, of course, prevent insofar as possible manipulation of prices to the detriment of actual investors, but at the same time we must eliminate unnecessary, unwise, and destructive speculation.

The bill, as shown to me this afternoon by you seems to meet the minimum requirements. I do not see how any of us could afford to have it weakened in any shape, manner, or form.

Very sincerely,

FRANKLIN D. ROOSEVELT.

2. The Necessity for Legislative Action

On March 2, 1932, Senate Resolution No. 84 was agreed to, authorizing the Committee on Banking and Currency (1) to make a thorough

and complete investigation of the practices with respect to the buying and selling and the borrowing and lending of listed securities upon the various stock exchanges, the value of these securities, and the effect of such practices upon interstate and foreign commerce, upon the operation of the national banking system and the Federal Reserve System, and upon the market for securities of the United States Government, and the desirability of the exercise of the taxing power of the United States with respect to any such securities, and (2) to report to the Senate as soon as practicable the results of such investigation and, if in its judgment such practices should be regulated, to submit with such report its recommendations for the necessary remedial legislation.

Pursuant to the resolution, an exhaustive investigation into stock exchange practices was conducted by the committee. Commencing on April 11, 1932, and at frequent intervals since that date, evidence gathered by its investigating staff has been presented to the committee at public hearings, which has laid the foundation for remedial legislation in a field heretofore unregulated.

The record compiled by the committee for the first time exposed methods by which a relatively small number of persons have extended their operations in securities far beyond any useful economic function, to the great detriment of the investing public. By the development of the margin account, a great many people have been induced to embark upon speculative ventures in which they were doomed to certain loss. The unfair methods of speculation employed by large operators and those possessing inside information regarding corporate affairs, and the failure of corporations to publish full and fair reports of their financial conditions, have also been contributing causes of losses to investors.

Excessive speculation has caused acute suffering and demoralization. It has brought in its train social and economic evils which have affected the security and prosperity of the entire country. During the boom period a vast and unhealthy volume of credit was sucked into securities markets to the deprivation of agriculture, commerce, and industry, which made possible the inflation of prices of securities out of all proportion to their value. Feverish speculation accelerated the process of inflation until the bubble burst in October 1929. The market value of all stocks listed on the New York Stock Exchange slumped from \$89,000,000,000 on September 1, 1929, to \$15,000,000,000 on July 1, 1932. There can be little question that stock-market speculation is among the most potent of the factors which have contributed to the prolonged depression.

The evidence submitted to the committee by experts on the staff of the Federal Reserve Board has indicated that uncontrolled speculation on security markets was an important cause of the credit inflation which led to the collapse of 1929 and the subsequent depression. Banks diverted their credit from agriculture, commerce and industry to the stock market, where it contributed to the over-expansion of big enterprises, largely engaged in interstate commerce. Corporations took advantage of the abnormal demand for securities by raising new capital, which was not necessary for plant expansion, but which they loaned in the call-money market, thus encouraging further speculation. When the crash finally came, brokers' loans were called, causing greater depreciation in the value of securities, including those held in bank portfolios. This contributed largely

to the widespread bank failures, which imperiled the national banking structure. Foreign money had also been attracted to the call market, and was subjected to heavy withdrawals which contributed to the panic and the hoarding of gold associated with the dislocation of the national currency system.

That the country has learned little from the catastrophe of 1929 is evidenced by the speculative boom during the summer of 1933, which ended with the usual disastrous results to investors. If our present progress toward prosperity is not to be impeded from time to time by the financial collapse invariably following artificial inflation of security prices, it is essential that the Federal Government adopt measures which will enable it to stem the speculative tide whenever necessary.

3. Inadequacy of Self-Regulation of Exchanges

Stock exchanges have hitherto resisted proposals for their regulation by any governmental agency, on the ground that they are sufficiently able to regulate themselves to afford protection to investors. Especially during periods of popular agitation, or when legislative action has been threatened, the exchanges have taken steps to raise the standards for the conduct of business by their members and to require corporations to furnish more adequate information for the benefit of investors. Such attempts, however, far from precluding the necessity for legislative action, emphasize its need.

The contention of stock exchange authorities that internal regulation obviates the need for governmental control seems unsound for several reasons. In the first place, however zealously exchange authorities may supervise the business conduct of their members, the interests with which they are connected frequently conflict with the public interest. Secondly, the securities exchanges have broadened the scope of their activities to the point where they are no longer isolated institutions, but have become such an important element in the credit structure of the country that regulation, to be effective, must be integrated with the protection of our entire financial system and the national economy. Thirdly, the control exercised by stock exchange authorities is admittedly limited to their own members, and they are unable to cope with those practices of nonmembers which they deplore but cannot prevent. Fourthly, the attitude of exchange authorities toward the nature and scope of the regulation required appears to be sharply at variance with the modern conception of the extent to which the public welfare must be guarded in financial matters. Their adherence to the view that manipulation, pool activities, and the creation of illusory "price mirages" are proper and legitimate, except where certain technical violations of their rules are involved, is inconsistent with the type of regulation the public interest demands.

The manipulation of the so-called "repeal stocks" on the New York Stock Exchange during the summer of 1933 illustrates the ineffectiveness of self-regulation. On July 18, 1933, there was a violent fluctuation downward in security prices led by the repeal stocks. A few days later counsel for the committee requested the exchange to institute an inquiry for the purpose of ascertaining whether pool operations were being conducted in repeal stocks between May 15,

1933, and July 24, 1933. On October 16, 1933, a report was rendered by the New York Stock Exchange detailing the results of its examination made in connection with trading and operations in the securities of 6 companies. The report stated "that there were no material deliberate improprieties in connection with transactions in these securities" and that there was no evidence of "activities which might have stimulated improperly the activity of these stocks." Thereupon the committee caused an independent inquiry to be made by its investigating staff and a series of hearings were held before the committee at which the evidence collected was made public. The record of these hearings is replete with proof of manipulation of security prices, of pool operations in which corporate officials participated and profited, and of unsavory practices in connection with the listing of securities. The inability of the stock exchange authorities even to discover the flagrant abuses unearthed by the committee indicates that a Federal regulatory body could deal with such practices more effectively than the exchanges themselves.

Although the exchanges have endeavored to bring about an improvement in the type of financial reports filed by corporations, they have been hampered by the terms of the listing contracts made with issuers, which they have not considered themselves entitled to modify without the consent of such issuers. Progress in this direction has been further retarded by the unwillingness of issuers to furnish adequate information, supported by the threat of withdrawal of their listings, and by the potential competition of exchanges having more lenient standards. Such impediments could not exist so far as a Federal regulatory body is concerned. The present bill would effectuate a reform which the exchanges themselves have been advocating for many years. Hence their efforts to enlist the opposition of corporations to the proposed legislation is difficult to reconcile with their public utterances in the past.

The three principal problems with which the bill deals are the excessive use of credit for speculation, the unfair practices employed in speculation, and the secrecy surrounding the financial condition of corporations which invite the public to purchase their securities.

II. GENERAL ANALYSIS OF THE BILL

1. Enforcing Agency and Flexibility of Procedure

From the outset, the committee has proceeded on the theory that so delicate a mechanism as the modern stock exchange cannot be regulated efficiently under a rigid statutory program. Unless considerable latitude is allowed for the exercise of administrative discretion, it is impossible to avoid, on the one hand, unworkable "strait-jacket" regulation and, on the other, loopholes which may be penetrated by slight variations in the method of doing business. Accordingly it is essential to entrust the administration of the act to an agency vested with power to eliminate undue hardship and to prevent and punish evasion. Of course, well defined limits must be indicated within which the authority of such administrative authority may be exercised.

The committee considers that the act could be administered effectively by a Commission of five, to be appointed by the President with the advice and consent of the Senate, specifically for that purpose.

In addition to the discretionary and elastic powers conferred on the administrative authority, effective regulation must include several clear statutory provisions reinforced by penal and civil sanctions, aimed at those manipulative and deceptive practices which have been demonstrated to fulfill no useful function. These sanctions are found in sections 9, 10, and 16. Moreover, the power to withdraw Federal registration is not a sufficient guarantee that the rules and regulations of the administrative authority, as well as the statutory provisions, will be observed; and accordingly the bill provides criminal penalties for violation of such rules and regulations. It is to be noted, however, that such penalties are limited to fines as distinguished from the penalties of imprisonment which may be inflicted for violation of the statutory provisions of the bill.

2. Registration of Exchanges

The bill forbids the use of the mails or instrumentalities of interstate commerce to any securities exchange which is not registered with the Commission as a "national securities exchange." The Commission, however, is empowered to exempt from registration small exchanges where the volume of transactions is not sufficient to invite the abuses prevalent on the larger markets. When applying for registration, exchanges must agree to comply with the act and with the rules and regulations of the Commission and to require observance of the same by their members.

In addition to the organized security markets, there exist in financial centers unorganized "over-the-counter" markets where securities are bought and sold in large volume. Many of these securities are of a conservative character, such as Government, State, and municipal bonds which are exempted from the provisions of the bill; but others are more speculative in nature and are subject to the abuses of manipulation. For example, the committee has heard evidence of extensive manipulation in certain New York bank stocks after their withdrawal from the New York Stock Exchange and while they were being sold "over the counter." These manipulations resulted in tremendous losses to the investing public, and in enormous profits to insiders. It has been deemed advisable to authorize the Commission to subject such activities to regulation similar to that prescribed for transactions on organized exchanges. This power is vitally necessary to forestall widespread evasion of stock exchange regulation by the withdrawal of securities from listing on exchanges, and by transferring trading therein to "over-the-counter" markets where manipulative evils could continue to flourish, unchecked by any regulatory authority. Since the necessity for regulation of "over-the-counter" markets will depend largely on the extent to which activities prohibited on exchanges are transferred to such markets, provision for their regulation has been made as flexible as possible.

3. Margins and Brokers Loans

Margin transactions involve speculation in securities with borrowed money. The ordinary procedure is for a broker to extend credit to his customer in order to finance the purchase of a security, the broker in turn borrowing from a banking institution or another broker. The ease and celerity with which such a transaction is arranged, and the absence of any scrutiny by the broker of the personal credit of the borrower, encourage the purchase of securities by persons with in-

sufficient resources to protect their accounts in the event of a decline in the value of the securities purchased. Many thoughtful persons have taken the view that the only way to correct the evils attendant upon stock market speculation is to abolish margin trading altogether. A Federal judge furnished this committee with instances from his long experience on the bench, indicating that a large proportion of business failures, embezzlements and even suicides in recent years were directly attributable to losses incurred in speculative transactions. The committee has deemed it unwise at this juncture to adopt a measure calculated to abolish margin trading because of the deflationary consequences which might follow. Nevertheless, it feels that the time has arrived to remove the control of credit in margin transactions from the hands of those who, by reason of their self-interest, are least qualified to administer such control—the stock exchanges and their members.

The original bill (S. 2693) contained rigid provisions limiting the amount of credit which could be extended on a registered security to 40 percent of the current market price or 80 percent of the lowest price during the preceding 3 years. After due consideration, the committee does not recommend that statutory limitations be placed upon the extension or maintenance of credit. The bill authorizes the Commission to prescribe rules and regulations for the purpose of preventing the excessive use of credit for the purchasing, selling, carrying or trading in securities. Such rules and regulations need not be uniform throughout the United States, and hence local conditions requiring special treatment may be taken into consideration. To prevent sudden liquidation of existing margin accounts subsequent to the passage of the bill, it is provided that the rules and regulations prescribed by the Commission shall not be effective before June 30, 1936, as to any loan made prior to the enactment of the bill, or any renewal thereof.

The foregoing provisions would be ineffectual to curb speculation unless they were supplemented by restrictions upon the power of others than brokers and dealers to extend credit, since loans to customers directly from banks and others could be arranged to evade margin requirements. The bill imposes manifold checks upon the employment of credit for speculative purposes: (1) It empowers the Commission to limit the amount of credit which a broker or dealer may extend upon a security; (2) it prohibits brokers and dealers from borrowing except through a member bank of the Federal Reserve System or in accordance with regulations of the Commission; (3) it empowers the Commission to limit the amount which brokers may borrow; (4) it authorizes the Federal Reserve Board to limit the amount which member banks may loan on securities; and (5) it empowers the Commission to regulate loans to brokers and dealers by corporations having securities listed on exchanges.

4. Manipulative Practices

Several devices are employed for the purpose of artificially raising or depressing security prices. Those which appear to serve no legitimate function are specifically prohibited. Among such practices are fictitious or "wash" sales; "matched" orders, or orders for the purchase and sale of the same security emanating from a common source for the purpose of recording operations on the tape and thereby

creating a false appearance of activity; and other transactions specifically designed to manipulate the price of a security.

The stock exchanges, and particularly the New York Stock Exchange, have contended that practices of this type are already prohibited by their rules. Yet testimony before the committee has shown that a broker, while operating a syndicate account in a copper stock, caused the sale of 35,000 shares by the syndicate and the purchase of 35,000 shares by an individual member of the syndicate on the same day. Although any intention to accomplish a "wash" sale was disclaimed, nevertheless the result of the transaction was to bring about an immediate rise in the market value of the stock from \$192 to \$196 a share with a handsome profit to the individual customer.

In another instance a syndicate purchased 1,130,000 shares of stock from an oil company. Simultaneously with the formation of the original syndicate, a trading syndicate was organized by the original participants for the purpose of "maintaining" the price of the stock until the commitment was disposed of. Both the original and the trading syndicates traded actively in the stock during the operation, buying and selling large blocks while avoiding technical "wash" sales. These operations were designed to give a fictitious appearance of activity to the market and to induce the public to purchase the stock and thereby relieve the original syndicate of its commitment. Through these means, the syndicate succeeded in unloading the stock at a profit of \$12,000,000 within a period of about 8 months.

The committee's record contains many examples of manipulation of prices through the medium of pools. Among these were the simultaneous operations of three pools in a radio stock, resulting in an aggregate profit to the participants of \$4,924,078. During the course of these operations, the price of the stock rose in a period of 4 days from 91% to 109%, at which point the pool withdrew its support and the price receded 3 days later to 96%, and 4 days later to 87%. Another pool operating in a copper stock over a period of 45 days realized a profit of \$1,225,768; and meanwhile the price rose from 116% to 163%. Manipulative practices such as the foregoing are prohibited by the present bill, under heavy penalties.

Other devices commonly resorted to in the past, and banned by the bill are the dissemination of false information and tipster sheets. The record shows that it was not uncommon for market operators to employ a publicity agent to tout a stock in which they were momentarily interested. In one instance a financial writer on a great New York newspaper was discovered to have been a regular participant in the profits of a free-lance trader, without obligation except to publicize the stocks of the trader. Another witness admitted that his business was "financial publicity", and that his articles were published for the purpose of interesting the public in the stock in which he and those who employed him were interested, thereby causing the market value of the stock to increase; and for this work he was paid by calls and options. Still other cases were observed where persons were employed to broadcast over the radio, ostensibly as economists tendering gratuitous advice, but in reality as publicity agents of stock-exchange firms.

The impropriety of practices such as "pegging" or fixing or stabilizing the price of a security has received most careful consideration

by the committee. The committee recommends that such practices be not abolished by statute but subjected to regulation by the Commission.

In like manner, the subject of options has been left with the Commission for regulation. Many of the most flagrant abuses upon stock exchanges would not be possible without the aid of options. They are indispensable concomitants of every pool operation designed to distribute stock at an increased price. Enormous profits have been made by operators who traded against options without incurring the slightest risk or obligation. The New York Stock Exchange a few months ago, at the suggestion of this committee's counsel, adopted a rule requiring its members to report regularly on options in which they are interested or of which they have knowledge by reason of transactions executed by or through them; but evasion of the rule is easily accomplished by causing the options to be granted to persons who are not members of the exchange or bound by its rules. Here again the necessity for regulation by a commission having authority over nonmembers as well as members of an exchange is evident.

Short selling has been defended as a necessary check upon a rising market and as a stabilizing factor in the ensuing decline; and attacked on the ground that it tends to unsettle the market, depress prices, and accelerate declines. The committee recommends that the practice of short selling be placed under the supervision of the Commission.

The bill further aims to protect the interests of the public by preventing directors, officers, and principal stockholders of a corporation, the stock of which is traded in on exchanges, from speculating in the stock on the basis of information not available to others. Any change in the holdings of such insiders must be reported to the Commission, and profits realized from the purchase and sale, or the sale and purchase of an equity security within a period of less than 6 months are recoverable by the corporation. Such a provision will render difficult or impossible the kind of transactions which were frequently described to the committee, where directors and large stockholders participated in pools trading in the stock of their own companies, with the benefit of advance information regarding an increase or resumption of dividends in some cases, and the passing of dividends in others. In a particularly glaring instance, the chairman of the executive committee and another director participated in a pool organized in trade in the stock of their company when the stock was paying no dividends. During the operation of the pool, which continued for a period of 2 years, they caused the company to resume the payment of dividends, more than 25 percent of which were received by the pool participants. These dividends were paid during the pool's operation in spite of the fact that the company's earnings were not sufficient to meet them and part of its surplus had to be diverted for that purpose. In another case, the president of a corporation testified that he and his brothers controlled the company with a little over 10 percent of the shares; that shortly before the company passed a dividend, they disposed of their holdings for upward of \$16,000,000 and later repurchased them for about \$7,000,000, showing a profit of approximately \$9,000,000 on the transaction. Many other instances were developed before the committee where insiders either personally or through the medium of holding companies participated largely in profits derived from the use of information not procurable by the investing public.

5. Corporate Reports

The information required to be filed under the Securities Act of 1933 relates only to the situation at the time a security is issued. Reports under this bill will provide adequate information reasonably up to date as long as the security is traded in on an exchange.

This aspect of the proposed legislation has been the target of an intensive campaign in the form of letters and telegrams addressed to Members of Congress and especially to members of this committee. The extent of the protest makes it worthy of serious consideration; but it appears that this opposition is largely based on a misunderstanding of the bill, the fear of exposure on the part of some corporations which have heretofore managed to withhold from investors their true financial condition, or the efforts of stock brokers hostile to other portions of the bill, who are endeavoring to marshal all possible aid in defeating the bill by inciting their customers to protest.

The principal objection directed against the provisions for corporate reporting is that they constitute a veiled attempt to invest a governmental commission with the power to interfere in the management of corporations. The committee has no such intention, and feels that the bill furnishes no justification for such an interpretation. To make this point abundantly clear, section 13 (d) specifically provides that nothing in the act shall be construed to authorize interference with the management of corporate affairs.

The bill provides that securities traded in upon exchanges must be registered with the Commission, and that a condition of such registration shall be the furnishing of complete information relative to the financial condition of the issuer, which information shall be kept up to date by adequate periodic reports. The Commission is given complete discretion not only to exempt securities from the operation of most sections of the act—including those dealing with corporate reports—but also to require in corporate reports only such information as it deems necessary or appropriate in the public interest or to protect investors. In this connection it should be noted that section 3 (a) (12) empowers the Commission to define "exempted securities" and sections 12 and 13 authorize it to vary the specifications for reports where those indicated are deemed inappropriate. Moreover, by section 23 a corporation is granted an unconditional right to a private hearing in any case where it feels that information filed with the Commission should not be made public, and by section 24, the Commission's determination on such hearing is subject to court review.

The argument has also been made that the provision for corporate reports will impose an undue burden on corporations by compelling them to keep their accounts in the manner prescribed by the Commission. The bill, however, merely permits the commission to specify the methods to be followed in preparing the reports made to it, and does not attempt to direct the manner in which the corporate books of account shall be kept. The only corporations apt to be seriously affected in this respect are those which do not keep even in their confidential files the information essential for the preparation of reports on which may be based an intelligent analysis of the value of their securities for investment purposes.

These provisions are regarded as the minimum which is requisite for the adequate protection of investors. The committee has repeatedly heard testimony illustrating the evasions, suppressions, distortions, exaggerations, and outright misrepresentations practiced by corporations with intent to cloak their operations and to present to the investing public a false or misleading appearance as to financial condition.

The chairman of the committee on stock list of the New York Stock Exchange testified that an application for listing of additional shares was granted to a corporation in June 1933; that while it was represented to the stock exchange authorities that the additional shares were to be issued in exchange for the shares of another corporation, no balance sheet of the latter was exhibited to the committee on stock list; and that had such balance sheet been presented, the listing would have been denied for several reasons, including the fact that it would have been discovered that the stock was being issued for the purpose of supplying capital, and not for the purpose of acquiring property as represented, the fact that the stockholders' preemptive rights were being circumvented, and the fact that practically all the assets of the company consisted of notes receivable, good will, and licenses arbitrarily valued at grossly exaggerated figures. The testimony also established that within a period of a few days the assets of the company were written up 100 percent in value. In another case brought to the attention of the committee, the assets of a company were marked up from \$4,000,000 to \$24,000,000. A memorandum prepared by a corporate official was introduced in evidence which discussed the alternatives of preparing the corporation's annual report in either the "standard" or the "understandable" form, the decision being in favor of the former. Many other instances of "window dressing" were observed, where inexcusable methods were employed to inflate assets, obscure liabilities, and conceal deficits.

6. Conduct of Brokerage Accounts

Severe financial losses have been sustained by investors from time to time in cases where a broker pledged his customers' securities for loans in excess of the aggregate indebtedness due him in respect of such securities, or pledged them along with his own securities to finance his private speculative commitments. These practices, as well as the loaning of a customer's security without written authority, are prohibited by the proposed bill.

Many critics of the stockbrokerage business as now conducted assert that a fundamental evil is the commingling of the functions of broker and dealer by the same person or firm. The contention has been advanced, and evidence before the committee has tended to prove, that a broker who deals in securities for his own account finds it difficult to give disinterested advice to a customer with regard to the securities the customer seeks to buy. However honest the broker's intentions may be, it is argued that he should be placed beyond temptation, by a complete segregation of the broker and dealer functions. The committee has reached the conclusion that for the present any such action would be unwise. Accordingly the bill directs the Commission to study the feasibility of the complete segregation of the functions of dealer and broker and to report its recommendations to the Congress prior to January 3, 1935.

Abuse of the dual function of principal and agent has been shown to be especially flagrant in the case of specialists. The bill leaves the regulation of specialists to the Commission, but directs that dealings by a broker specialist for his own account shall be reasonably limited. The bill also authorizes the Commission to regulate floor trading, a practice which enables speculators on the scene of activities to indulge in many manipulative devices and to demoralize the market in times of excessive trading.

One situation exists in which the combining of the functions of dealer and broker results in such clear abuse that it has been deemed advisable to include a statutory prohibition. The bill forbids any person who is both a broker and a dealer to use an exchange, the mails, or instrumentalities of interstate commerce, to effect any transaction involving the sale on margin, of a security in the distribution of which he has participated during the preceding 6 months. While a dealer is assisting in the distribution of a new issue, he is most strongly tempted to persuade his customers to invest in it. A broker is also required to disclose in writing to a customer, any interest which he has in the transaction, in such manner as the Commission may prescribe, failing which disclosure, the customer may disaffirm the transaction within 10 days.

7. Proxies

In order that the stockholder may have adequate knowledge as to the manner in which his interests are being served, it is essential that he be enlightened not only as to the financial condition of the corporation, but also as to the major questions of policy, which are decided at stockholders' meetings. Too often proxies are solicited without explanation to the stockholder of the real nature of the questions for which authority to cast his vote is sought. For example, in one case brought to the committee's attention, proxies were solicited by the president of a corporation by means of a letter which purported to describe certain transactions concerning which ratification by the stockholders was sought. The letter omitted all mention of other important details such as previously granted secret options in the corporation's stock, and the president's individual interest in an underwriting agreement made by the corporation, which furnished the real motive behind the request for ratification. The solicitation in that case so far succeeded that not a single stockholder appeared at the meeting in person, and an employee of the company voted all proxies in favor of ratifying all acts and proceedings taken by the directors and officers of the corporation. The committee recommends that the solicitation and issuance of proxies be left to regulation by the Commission.

8. Civil Liabilities

Experience with State laws designed to prevent the exploitation of the investor by supervision of the sale of securities has demonstrated the inadequacy of criminal penalties as the sole sanction. Customers are ordinarily reluctant to resort to criminal proceedings, and in the absence of complaints by them, the discovery of violations is often impossible. Furthermore, if an investor has suffered loss by reason of illicit practices, it is equitable that he should be allowed to recover damages from the guilty party. With these considerations in view, the bill provides that any person who unlawfully manipulates the price

of a security, or who induces transactions in a security by means of false or misleading statements, or who makes a false or misleading statement in the report of a corporation, shall be liable in damages to those who have bought or sold the security at prices affected by such violation or statement. In such case the burden is on the plaintiff to show the violation or the fact that the statement was false or misleading, and that he relied thereon to his damage. The defendant may escape liability by showing that the statement was made in good faith. The party sued may recover contribution from any other person who would also be liable with respect to the same subject matter if separately sued.

9. Administrative Machinery

Disciplinary action short of criminal or civil penalties is provided for in section 19. The Commission is authorized in case of certain violations and after adequate hearing, to suspend or withdraw the registration of an exchange or of a security, and to suspend or expel a member or officer of an exchange. In an emergency the Commission may suspend trading in a security for 10 days, or, with the consent of the President of the United States, close an exchange for 90 days.

The Commission is empowered, after an exchange has failed to adopt rules governing the conduct of business by its members which the Commission deems necessary for the protection of investors, to order such adoption. Thus the initiative and responsibility for promulgating regulations pertaining to the administration of their ordinary affairs remain with the exchanges themselves. It is only where they fail adequately to provide protection to investors that the Commission is authorized to step in and compel them to do so.

The Commission is also charged with responsibility for investigating violations of the act and of the rules and regulations thereunder. One of the greatest obstacles to enforcement of statutes governing the activities of brokers in some States, is the lack of provision requiring adequate records of transactions. Section 17 of the bill requires that exchanges, their members, and brokers, and dealers doing business through them, must preserve such records of their transactions as the Commission may require, and must keep them available for reasonable inspection by the Commission. In this manner the Commission will be able to obtain evidence rapidly in any case where fluctuations in the price of a security indicate that manipulation may be in progress.

Any person aggrieved by an order of the Commission in a proceeding to which he is a party, may obtain a court review of the Commission's action.

10. No Official Approval of the Value of Securities

As pointed out above, there is no intention whatsoever to permit the Commission to direct the flow of credit or to determine what securities shall be issued or sold. On the contrary, it is expressly provided that no action, or failure to act, by the Commission as to any security or transaction shall be construed as an approval of the security or transaction in question, and it is made unlawful to represent to any prospective purchaser or seller that any such action or failure to act by the Commission is subject to such a construction.

III. SUMMARY OF THE BILL BY SECTIONS

Section 1. Short Title

This section gives the title of the act as the "Federal Securities Exchange Act of 1934."

Section 2. Necessity for Regulations as Provided in this Act

This section contains a general declaration of the purposes and objects of the bill.

Section 3. Definitions and Application of the Act

Subsection (a) defines the terms used in the act. Most of these definitions are self-explanatory. The most important are those of the terms "broker" and "dealer" in paragraphs (4) and (5), since many of the provisions of the act apply only to members of exchanges and brokers and dealers who do business through them. A broker is defined as a person engaged in the business of effecting transactions for the account of others; and a dealer as one engaged in such business for his own account, but only insofar as his transactions are in the course of a regular business. Furthermore, banks are expressly exempted from the definitions of "broker" and "dealer." The definition of "bank" in paragraph (6) includes banks organized under the laws of the United States, members of the Federal Reserve System, and any other bank performing normal banking functions which is subject to supervision and examination by State or Federal authorities.

The definitions of "issuer" and "security" are substantially the same as those in the Securities Act of 1933.

An "exempted security" is defined in paragraph (12) to include obligations guaranteed as to principal or interest by the United States or any State or political subdivision thereof. In addition the Secretary of the Treasury may designate for exemption the securities of corporations in which the United States has a direct or indirect interest; and the Federal Securities Exchange Commission (elsewhere referred to as the "Commission") is given power to place in the category of "exempted securities" any other securities (including unregistered securities the market in which is predominantly intrastate) where it deems such action necessary or appropriate in the public interest or for the protection of investors. A large number of the provisions in the Act expressly exclude "exempted securities." Thus the Commission is able to remove from the operation of any one or more of these provisions any securities as to which it deems such provisions inappropriate. It may attach such conditions to such exemptions as it deems desirable.

Subsection (b) provides that the act shall not apply to instrumentalities and agencies of the United States.

Section 4. Federal Securities Exchange Commission.

Subsection (a) provides for the creation of a Federal Securities Exchange Commission to be composed of five members appointed by the President, by and with the advice and consent of the Senate. Not more than three shall be members of the same political party and appointments shall be made, as far as practicable, alternately from members of different parties. Commissioners are not permitted to engage in any other vocation or employment, nor to participate in

any way in stock market operations of the type which are subjected to regulation by the commission pursuant to this act. The Commissioners are to receive \$12,000 a year and regular appointments shall be for terms of 5 years, one expiring each year.

Subsection (b) authorizes the Commission to make such rules and regulations as may be necessary for discharging the duties imposed on it under this act. Different provisions may be made for different classes of persons, securities, or exchanges within their scope. The Commission is also authorized to define accounting, technical and trade terms used in the act, provided that the definitions be not inconsistent with the act.

Subsection (c) authorizes the Commission to appoint and fix the compensation of such employees as may be necessary for performing its functions under the act without regard to civil-service laws.

Subsection (d) provides that the expenses of administering the act shall be borne by the exchanges subject to it.

Section 5. Transactions on Unregistered Exchanges

This section forbids the use of the mails and instrumentalities of interstate commerce to any exchange which is not registered as a "national securities exchange" under section 6, but authorizes the Commission to exempt from this prohibition any small exchange as to which it finds that registration would be impracticable and unnecessary.

Section 6. Registration of National Securities Exchanges

Subsection (a) provides for registration as a "national securities exchange" upon application by any exchange which agrees to comply, end to require its members and the issuer of the securities it deals in to comply, with the act and the rules and regulations thereunder and furnishes the Commission with complete information concerning its organization, membership, and rules.

An exchange is also required by subsection (b) to provide for the disciplining of members who are guilty of conduct "inconsistent with just and equitable principles of trade", and must include in this category any willful violation of this act or any rule or regulation thereunder.

It is provided in subsection (c) that exchanges may adopt any rules not inconsistent with the act or rules and regulations.

Subsection (d) directs the Commission to grant an application for registration made pursuant to this section, if it appears that the exchange is so organized as to be able to comply with the act and rules and regulations and to insure fair dealing and the protection of investors.

Subsection (e) provides that the Commission's order granting or denying an application for registration shall be made within 30 days unless the application has been withdrawn.

Subsection (f) permits an exchange to withdraw its registration upon such terms as the Commission may deem necessary for the protection of investors.

Section 7. Margin Requirements

By subsection (a) members of registered exchanges and brokers and dealers who do business through them are forbidden to extend or maintain credit to customers in contravention of the rules and

regulations of the Commission. Such rules and regulations shall be designed to prevent the excessive use of credit for security transactions. They may fix the amount of credit to be initially extended or maintained on any registered securities other than exempted securities. Appropriate provision may be made for such details as withdrawals, substitutions, additional purchases, transfers of accounts, delayed deliveries, departure from margin requirements for limited periods, methods of calculation, etc. They need not be uniform throughout the United States.

Subsection (b) authorizes the Commission to make rules and regulations so far as may be necessary to prevent evasion of this section through loans from persons who are not members of the exchanges, brokers or dealers, or members of the Federal Reserve System. It is expressly provided that such regulations shall not apply to loans not made in the ordinary course of business (such as purely personal loans), to loans on exempted securities, to loans to aid dealers in the distribution of securities not through the medium of a national securities exchange, to bank loans on any security other than an "equity security", or to such other loans as the Commission may deem it necessary or appropriate to exempt.

Subsection (c) makes the provisions of this entire section inapplicable to credit outstanding at the effective date of this act until June 30, 1936. This is designed to prevent forced liquidation.

Loans by member banks of the Federal Reserve System are covered by subsection (d) which gives the Federal Reserve Board the power to prescribe margin requirements for such loans, and imposes fines for violations.

Section 8. Restrictions on Borrowing by Members, Brokers, and Dealers

By subsection (a) borrowings on registered securities (other than exempted securities) by members, and brokers and dealers who do business through them, are confined to loans from member banks of the Federal Reserve System and loans from other sources made in accordance with such rules as the Commission may prescribe, either in general or under particular conditions.

Subsection (b) prohibits a member, broker, or dealer to permit his indebtedness (except on exempted securities) in the ordinary course of business as a broker to exceed 2,000 percent of his net capital or such lower percentage thereof as the Commission may prescribe.

A broker is prohibited by subsection (c) to commingle the securities of customers without their written consent; and regardless of such consent to pledge customers' securities with those of persons who are not customers or under circumstances that will subject customers' securities to a lien in excess of the aggregate indebtedness of the customers. He is also forbidden by subsection (d) to lend a customer's securities without the latter's written consent.

Section 9. Prohibition Against Manipulation of Security Prices

Subsection (a) makes it unlawful for any person to use the mails, interstate commerce, or any facility of a national securities exchange, or for any member of a national securities exchange by use of any means, to participate in certain practices in connection with securities registered on a national securities exchange, or to "effect" certain

transactions therein. In this and other sections of the bill "effect" refers to participation in a transaction whether as principal, agent, or both. The practices covered by this section include those commonly resorted to by manipulative pools.

Paragraph (1) forbids any fictitious purchases or sales, commonly known as "wash" sales.

Paragraph (2) makes it unlawful to buy and sell at substantially the same time, substantially the same amount of the same security for the purpose of causing a misleading appearance as to the real nature of the market or activity of trading in the security. This includes what are known as "matched" orders.

To manipulate the price of a security by any series of transactions with the specific intent of raising or depressing the price, is prohibited by paragraph (3). Any extensive purchases or sales are bound to cause changes in the market price of the security, but mere knowledge on the part of the purchaser or seller that his transactions will have this effect is not sufficient to bring him within the scope of this provision. Thus, if a person is merely trying to acquire a large block of stock for investment, or desires to dispose of a big holding, his knowledge that in doing so he will affect the market price does not suffice to make his actions unlawful.

Paragraph (4) makes it unlawful for the purpose of inducing the purchase or sale of a security to make statements which are false or misleading in a material respect or to make material omissions.

Paragraph (5) makes it unlawful to circulate for a consideration predictions or opinions that a security will change in price as a result of market operations by any persons, or to pay, or receive consideration for so doing. This provision is aimed at the "tipster sheet" and the practice of customer's men in inducing customers to buy or sell by spreading rumors with regard to the operations of pools.

The "pegging" of security prices is left to regulation by the Commission under paragraph (6) as it may deem necessary for the prevention of activities detrimental to the interests of investors.

Subsection (b) deals with options, which have been a common feature of pool operations. Their use is made unlawful only when in violation of such rules and regulations as the Commission may deem necessary in the interests of investors, governing the use of exchange facilities in trading in or against any option with regard to the security involved, or in giving options.

Subsection (c) empowers the Commission to make regulations regarding the guaranteeing of options for registered securities by members of national security exchanges.

Subsection (d) makes it clear that the options to be regulated under subsections (b) and (c) which include so-called "puts", "calls", "straddles", and "privileges"—which are commonly used for manipulative and speculative purposes—do not include warrants or rights to subscribe to a security or the right of the holder of a convertible security to have it converted.

Subsection (e) provides that persons who willfully participate in the manipulative or speculative practices which are forbidden by subsection (a), (b), and (c) shall be liable for the damages they cause to innocent investors who have bought or sold the security in question at a price which has been effected by such unlawful practices.

In order to give protection against "strike" suits, or litigation brought in bad faith, the court is authorized to assess reasonable costs, including attorney's fees against either party to the suit, and even to require in advance an undertaking for the payment of such costs. If the suit is brought by a party who has been induced to buy or sell a security by a false or misleading statement with regard to it, in violation of paragraph (4), the defendant may escape liability even if the statement was false or misleading if he can prove that he acted in good faith. A defendant may recover contribution from any other participant in the illegal transactions, who would have been liable if separately sued. Suits for recovery under this subsection must be commenced within 2 years after discovery of the violation, and, in any case, within 6 years of its occurrence.

Subsection (f) exempts from the operation of section 9 all "exempted securities".

Section 10. Regulation of the Use of Manipulative and Deceptive Devices

The scope of the section is confined to transactions effected by the use of the mails, the instrumentalities of interstate commerce, and the facilities of a national securities exchange.

Subsection (a) subjects to regulation by the Commission short sales and the use of stop loss orders, which greatly facilitate speculation.

Subsection (b) authorizes the Commission by rules and regulations to prohibit or regulate the use of any other manipulative or deceptive practices which it finds detrimental to the interests of the investor.

Section 11. Restrictions on Floor Trading by Members

Subsection (a) directs the Commission to regulate or prevent floor trading on the part of members. By such regulations those who are actually on the scene of speculation may be restricted from taking undue advantage of this privilege. The Commission is also directed by rules and regulations to prevent such excessive speculation on the part of members who operate from off the floor as it may deem detrimental to the maintenance of a fair and orderly market. The Commission may make such exemptions as are necessary or appropriate in the case of "exempted securities" and transactions by odd-lot dealers and specialists.

Subsection (b) authorizes the registration of members as odd-lot dealers or specialists, or both, pursuant to the rules of the exchange, and subject to rules and regulations of the Commission. As an odd-lot dealer a member shall be permitted to deal for his own account only so far as reasonably necessary in the performance of this particular function, and the Commission is directed to limit a member's dealings for his own account as specialist to those which are necessary for the maintenance of a fair and orderly market. The specialist is forbidden to reveal the orders on his books to favored persons. This information must be available to all members or else kept entirely confidential. The specialist is likewise prohibited from exercising purely discretionary orders as distinct from market or limited price orders.

Subsection (c) authorizes the Commission to exempt small exchanges from the provisions of this section.

Subsection (d) provides that any member, or any person doing business through a member, who acts both as a broker and dealer shall

not use the mails, or instrumentalities of interstate commerce, or any national securities exchange to effect any transaction which involves purchasing for a customer on margin, or selling to him on margin, any security which the broker or dealer has been engaged in distributing within 6 months.

Subsection (e) directs the Commission to investigate and report to Congress by January 3, 1935, on the question of completely segregating the activities of brokers and dealers.

Section 12. Registration Requirements for Securities

Subsection (a) prohibits members, brokers, and dealers from effecting any transaction on a national securities exchange in any security which is not exempted or registered under the provisions of the act.

The application to be filed by the issuer of a security with the exchange and with the Commission as a prerequisite to registration is described in subsection (b). Pursuant to paragraph (1) the issuer must agree to comply with the act and rules and regulations thereunder and not to lend any funds on other than exempted securities on any exchange or to any members thereof or brokers and dealers doing business through them except in accordance with the rules and regulations of the Commission. Member banks of the Federal Reserve System are exempted from this provision since their activities on the money market are subject to regulation by the Federal Reserve Board.

In paragraph (2) is indicated the information which the Commission may require an issuer to file in its application for registration.

Under paragraph (3) copies of various documents, such as articles of incorporation, bylaws, and underwriting arrangements, are required to be filed.

Subsection (c) authorizes the Commission if it deems any of the information specified under subsection (b) to be inappropriate in a given case or class of cases to require in lieu thereof the submission of other information of a comparable character.

If an exchange approves the registration of a security and so certifies to the Commission, the Commission is required by subsection (d) to approve the registration within 30 days. No authority is given the Commission to refuse registration for any reason other than failure to comply with the conditions authorized by this act. An issuer may cancel its registration on 30 days' notice, except that the Commission may require ratification by a majority vote of the stockholders if it deems such action necessary for the protection of investors. Registration of unissued securities for trading on a "when, as, and if issued" basis is permitted subject to regulations of the Commission in cases where the primary purpose of the registration is not to distribute the security to investors other than the present security holders of the company.

The Commission is authorized by subsection (e) to extend registration to securities already listed on exchanges without compliance with the registration requirements set forth in this section. Such registrations may be effective until June 1, 1935.

Subsection (f) provides that unlisted trading may be permitted by the rules and regulations of the Commission until June 1, 1936, in securities admitted to unlisted trading before March 1, 1934. Such securities are to be regarded as registered securities under this act,

except that they may be exempted from the requirements of this section and 13, but in quoting transactions exchanges must specify the securities which are admitted merely to unlisted trading.

Section 13. Periodical and Other Reports

Subsection (a) authorizes the Commission to require the issuers of registered securities to keep the information filed under section 12 reasonably up to date and to make annual reports, certified by independent public accountants if the Commission deems this necessary, quarterly reports, and such other reports as may be deemed essential under special circumstances.

Subsection (b) permits the Commission to specify the form in which reports shall be made, the details to be shown in financial statements and the methods to be followed in preparing the information to be included in such reports, but conflict with the reporting requirements under any other law of the United States is precluded.

Subsection (c) corresponds with subsection (c) of section 12 and permits the Commission to substitute comparable requirements where those indicated seem inappropriate.

Subsection (d) provides that nothing in the act shall be construed to authorize the Commission to interfere with the management of the affairs of an issuer.

Section 14. Proxies

Subsection (a) prohibits the solicitation of proxies in respect of securities (other than exempted securities) registered on a national securities exchange in contravention of such rules and regulations as the Commission may adopt for the protection of investors, but this does not apply to the mere submission of a form of proxy for the convenience of stockholders.

Subsection (b) imposes a similar restriction upon the giving of proxies by members, brokers, or dealers with respect to securities registered on a national securities exchange and carried for the account of customers.

Section 15. Over-the-Counter Markets

The use of the mails and instrumentalities of interstate commerce for the creation of markets other than regular exchanges is made the basis for such regulation of these markets as the commission may find appropriate to insure to investors protection comparable to that which is accorded in the case of registered exchanges under the act. Such rules and regulations may include provision for the registration of brokers and dealers and of the securities traded. Securities already traded in on exchanges at the time the act becomes effective may be subjected to special regulation if they do not become registered under section 12.

Section 16. Directors, Officers, and Principal Stockholders

Under subsection (a) directors and officers of the issuer of a registered security, and holders of more than 10 percent of any class of a registered equity security (other than an exempted security), are required at the time of registration of such security to file with the Commission a list of their holdings of the issuer's securities, and to report any change of ownership occurring during any month.

Subsection (b) makes available to the issuer profits realized by directors, officers, and principal security holders (as defined in sub-

section (a)) derived from sales and purchases within a period of 6 months or less. The expressed purpose of this provision is to prevent the unfair use of inside information. The Commission may exempt transactions not falling within this purpose.

By subsection (c) directors, officers, and principal stockholders are forbidden to sell registered securities (other than exempted securities) short, or for delivery after 20 days.

Subsection (d) exempts arbitrage transactions from the provisions of this section if such transactions are not in contravention of the rules and regulations of the Commission.

Section 17. Accounts and Records, Reports, Examination of Exchanges, Members, and Others

National securities exchanges, their members, brokers and dealers, and brokers and dealers who maintain over-the-counter markets, are required to keep such records as the Commission may prescribe in the public interest or for the protection of investors. These records shall be open to reasonable inspection by the Commission.

Section 18. Liability for Misleading Statements

Subsection (a) provides that any person who makes any statement which is false or misleading in any material respect shall be liable to a person who in reliance on the statement and in ignorance of its false or misleading character has purchased the security to which it relates at a price affected by it, unless the person sued proves that he acted in good faith without knowledge of the false and misleading character of the statement. Protection against strike suits is provided by giving the court authority in its discretion to assess costs, including attorney's fees, against either party and even to require an undertaking for the payment thereof. An omission of a material fact constitutes a misleading statement.

Subsection (b) provides for contribution between persons who would be liable if sued separately, and subsection (c) limits the time for bringing suit to 2 years after discovery of the facts, and, in any case, to 6 years after their occurrence.

Section 19. Disciplinary Powers over Exchanges.

Subsection (a) authorizes the Commission when it deems such action necessary (1) to suspend for not more than 12 months or withdraw registration of an exchange which has violated the act or the rules and regulations thereunder or has failed to take adequate steps to enforce the same; (2) to suspend for not more than 12 months, or to withdraw the registration of a security of, an issuer who has failed to comply with the act or rules and regulations thereunder; (3) to suspend for not more than 12 months or expel a member or officer of an exchange who is guilty of a violation or of aiding a violation by acting for a person who, he has reason to believe, is engaged in a violation; and (4) summarily to suspend all trading in any registered security for a period not exceeding 10 days or with the approval of the President of the United States summarily to suspend all trading on a registered exchange for not more than 90 days. Orders issued pursuant to (1), (2), and (3) must be preceded by appropriate notice and opportunity for hearing; action under (4) is of an emergency nature and, therefore, may be exercised summarily.

Subsection (b) authorizes the Commission after an exchange has failed to comply with its written request for an amendment of the

exchange's rules which the Commission deems necessary or appropriate for the protection of investors or to insure fair dealing or administration of the exchange, by order to amend the exchange's rules.

Subsection (c) directs the Commission to make a study of the administration and management of exchanges (including disciplinary action) and to report to Congress by January 3, 1935.

Section 20. Liabilities of Controlling Persons

By subsection (a) a person who controls a person subject to the act or a rule or regulation thereunder is made liable to the same extent as the person controlled unless the controlling person acted in good faith and did not induce the act in question.

Subsection (b) makes it unlawful for any person to do through any other person for the purpose of avoiding a provision of the act, anything that he is forbidden to do himself.

Subsection (c) makes it unlawful for a director, officer, or security owner unreasonably to hinder, delay or obstruct the making of reports or the filing of information required of an issuer under the act.

Section 21. Investigations; Injunctions and Prosecutions of Offenses

Subsection (a) authorizes the Commission to investigate and make public any facts regarding any violations, and to make investigations necessary to serve as a basis for enforcing the act, prescribing rules and regulations, and recommending further legislation.

Subsection (b) describes the Commission's power to compel the attendance of witnesses and production of evidence.

Subsection (c) authorizes the Commission to sue in United States courts for an injunction against a threatened violation.

Subsection (d) authorizes United States Courts on application of the Commission to compel obedience to the act or orders of the Commission by writs of mandamus.

Section 22. Hearings by Commission

This section provides that hearings before the Commission and its representatives may be public and that appropriate records are to be kept.

Section 23. Public Character of Information

Subsection (a) authorizes the Commission to make public such information as it deems necessary or appropriate in the public interest, or for the protection of investors and not in violation of trade secrets, but prior to disclosure, any person who has filed information may apply for a private hearing in which to give reasons why the disclosure should not be made.

Subsection (b) makes it unlawful for members of the Commission's staff to reveal information which has not been made public.

Section 24. Court Review of Orders

Any party to a proceeding under this act who is aggrieved by an order of the Commission is entitled to a review thereof in a Circuit Court of Appeals or the Court of Appeals of the District of Columbia. The Commission's findings of facts are conclusive if supported by substantial evidence. Provision is made for the adducing of new evidence discovered after the Commission's order.

Section 25. Unlawful Representations

No action or inaction by the Commission is to be construed as a passing on the merits of any transaction or the truth of any report. It is unlawful to represent to any prospective purchaser or seller that such action or inaction is to be so construed.

Section 26. Jurisdiction of Offenses and Suits

Enforcement of the act is confined by subsection (a) to United States courts and provision is made regarding the district in which a suit may be brought.

Subsection (b) authorizes the court to order a refractory witness to appear before the Commission.

Subsection (c) removes the defense of self-incrimination but exempts witnesses from prosecution for matters concerning which they have been compelled to testify.

Section 27. Effect on Existing Law

Subsection (a) provides that rights and remedies under the act shall be in addition to those already existing. The jurisdiction of State securities commissions remains unaffected insofar as it does not conflict with the act or rules and regulations thereunder.

Subsection (b) provides that the binding effect of action taken by the authorities of an exchange on members or other persons who have agreed to be bound thereby shall not be impaired by the provisions of the act or rules and regulations thereunder, if not inconsistent with such provisions.

Section 28. Validity of Contracts

Subsection (a) makes void any agreement to waive any compliance with the act or rules and regulations thereunder.

Subsection (b) provides that contracts made in violation of the act or rules and regulations thereunder shall be void. Contracts made before the effective date of the act shall be void as regards performance after such date insofar as such performance is inconsistent with the act or rules and regulations thereunder.

Subsection (c) is designed to prevent hardship resulting from the provisions of subsections (a) and (b). It provides that persons acquiring obligations in good faith for value and without actual knowledge of facts making them illegal, shall not be affected by such illegality.

Section 29. Foreign Securities Exchanges

Subsection (a) makes it unlawful for brokers and dealers to use the mails or instrumentalities of interstate commerce to effect on foreign exchanges transactions in American securities in contravention of the rules and regulations of the Commission.

Subsection (b) provides that nothing in the act or rules and regulations shall apply to business in securities outside the jurisdiction of the United States unless such rules and regulations expressly so provide in order to prevent evasion.

Section 30. Penalties

Under subsection (a) wilfully violating the act, or wilfully and knowingly making a false or misleading statement, will subject the offender to a fine of not more than \$25,000 and imprisonment of not more than 5 years, or both, except that if the offender is an exchange a fine of not exceeding \$500,000 may be imposed.

By subsection (b) the violation of a rule or regulation or of an agreement made with the Commission is punishable by a fine of not more than \$10,000, or in the case of an exchange not more than \$100,000.

Section 31. Separability of Provisions

This section provides for the separability of the provisions of the act in case any part thereof is held invalid.

Section 32. Effective Date

Provisions regarding the setting up of administrative machinery are made effective immediately. Applications for registration may be made on and after September 31, 1934, and may become effective on or after October 1, 1934, on which date sections pertaining to registered securities become effective.

TO ADD CERTAIN LANDS TO THE PIKE NATIONAL FOREST, COLO.

APRIL 17 (calendar day, APRIL 23), 1934.—Ordered to be printed

Mr. WAGNER, from the Committee on Public Lands and Surveys, submitted the following

REPORT

[To accompany H.R. 2858]

The Committee on Public Lands and Surveys, to whom was referred the act (H.R. 2858) to add certain lands to the Pike National Forest, Colo., having considered the same, report favorably thereon with the recommendation that the act do pass without amendment.

The facts concerning the proposed legislation are set forth in the report of the House Committee on the Public Lands (H.Rept. No. 988, 73d Cong., 2d sess.), as follows:

The Committee on the Public Lands, to whom was referred the bill (H.R. 2858) providing for the addition of lands to the Pike National Forest in Colorado, having considered same, report favorably thereon and recommend that the bill do pass with the following amendment:

Page 2, line 20, insert the following:

"Township 12 south, range 77 west, sixth principal meridian, west half southwest quarter section 11; west half northwest quarter, west half southwest quarter, southeast quarter southwest quarter section 14; northwest quarter section 23; southwest quarter section 26; north half section 34, and northwest quarter section 35.

"Township 13 south, range 77 west, sixth principal meridian, west half southwest quarter section 2; south half section 3; all section 10; west half northwest quarter and west half southwest quarter section 11."

The Department of Agriculture and the Department of the Interior recommend the enactment of the proposed legislation, and their letters are herein set out in full and made a part of this report.

DEPARTMENT OF AGRICULTURE,
Washington, February 6, 1934.

HON. RENÉ L. DEROUEN,
Chairman Committee on the Public Lands,
House of Representatives.

DEAR MR. DEROUEN: Reference is made to your letter of January 25, enclosing a copy of H.R. 2858, a bill to add certain lands to the Pike National Forest, Colo., and asking for a report thereon.

The proposed legislation would add to the Pike National Forest certain described lands comprising an area of approximately 7,360 acres. These lands lie