INDEX

<table>
<thead>
<tr>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Certain Fraudulent Acts Illustrated by SEC Release</td>
</tr>
<tr>
<td>District Activities</td>
</tr>
<tr>
<td>Questions and Answers</td>
</tr>
<tr>
<td>Secretaries, Counsel Meet</td>
</tr>
<tr>
<td>Sumner T. Pike Biography</td>
</tr>
<tr>
<td>Typical Complaints</td>
</tr>
<tr>
<td>Violations of SEC Rule X-17A-3 Revealed</td>
</tr>
</tbody>
</table>

SEC INVESTIGATIONS

REVEAL REAL VIOLATIONS

Many Members Misunderstand Regulations on Keeping and Preservation of Records

It has been learned that SEC investigations reveal numerous violations by Association members of SEC Rules X-17A-3 and X-17A-4 (Keeping and Preservation of Records). These violations generally occurred among the smaller firms. This apparently results from considerable confusion as to how these rules must be physically complied with. For this reason, the Washington office of the NASD has sent to all District Chairmen certain forms prepared by Tallman, Robbins & Co., which are designed to accomplish simple and convenient compliance with the Rules.

Forms Available for Inspection

These forms are available for the inspection of any member who desires to see them. Further information concerning the forms may be obtained from Tallman, Robbins & Co., 314 West Superior St., Chicago, III.

Apart from physical compliance with the Rules, there also appears to be some confusion as to whom the Rules are applicable. They apply not only to certain members of national securities exchanges, but also to all brokers and dealers registered with the SEC.

The provisions of the Rules are explained in Pages E-1-13 of your MANUAL. The Rules themselves, are contained at Pages E-14-17.

SEC RELEASE ILLUSTRATES CERTAIN TYPES OF ACTS REGARDED AS FRAUDULENT

Complaint Charges Securities Dealers Claimed Wide Experience When They Had Little

Commission Reports in Injunction Case

The following release of the Securities and Exchange Commission is well worth reading as an illustration of certain broker-dealer conduct which ran afield of certain fraud provisions of the Securities Act of 1933 and the over-the-counter provisions of the Securities and Exchange Act of 1934.

(Exroth's Note: The names of the persons actually involved in the case have been deleted by us and the letters A, B and C inserted in their stead.)

"The Securities and Exchange Commission today reported that Judge — of the United States District Court for the — had entered a final judgment enjoining Mr. A, Mr. B and Mr. C from further violating the fraud provisions of the Securities Act of 1933. The Court also enjoined Mr. A from further violating the over-the-counter market provisions of the Securities Exchange Act of 1934. The defendants consented to the entry of the judgment.

"The Commission in its complaint alleged that since January 1, 1938, the defendant A had been effecting transactions in securities and inducing their purchase and sale by means of deceptive and fraudulent devices and contrivances in violation of Section 18 (c) of the Securities and Exchange Act of 1934.

Practices Alleged by SEC

"In this connection, it was alleged that A, among other things, purported to act as a broker or agent in the purchase and sale of securities for the account of his customers, when in fact, without their knowledge, approval or consent, he acted as principal; that while purporting to act as agent in purchasing securities for his customers, he charged them an amount far in excess..."
QUESTIONS AND ANSWERS

QUESTION: What are the obligations of a member when acting as a broker for his customer as distinguished from a member's obligations when he acts as a dealer in a transaction with a customer?

ANSWER: It is not possible in the compass of this column fully to answer all of the legal and other implications of this question but the following observations are by way of a general reply.

When a member acts as a broker for his customer, he either buys or sells securities for his customer, and for services rendered he is entitled to charge a commission. Acting in this capacity, a member is no more nor less than a simple agent of his principal, the customer whose orders he executes. As such an agent, his general obligations are well defined by the common law.

A Broker's Duties

Essentially, a broker or agent is a fiduciary and he thus stands in a position of trust or confidence with respect to his customer or principal. He must at all times, therefore, think and act as a fiduciary. He owes his customer or principal complete obedience, complete loyalty, and the exercise of his unbiased judgment. The law will not permit a broker or agent to put himself in a position where he can be influenced by any considerations other than those to the best interests of his customer or principal. Thus, when acting as a broker for his customer with respect to a transaction in Security A, he can not himself buy Security A from his customer or himself sell Security A to his customer. Nor can a member act as a broker for two customers in connection with the same transaction unless he makes full disclosure to both customers of the true nature of his position.

Secret Profits Barred

A broker may not in any way, nor in any amount, make a secret profit. For example, a broker may not, directly or indirectly, purchase or sell a security for his customer at one price and confirm the purchase or sale to his customer at a different price and retain any difference. He must confirm to his customer at the price at which he purchases or sells the security, plus, of course, his commission, if any, for services rendered, which, under the Rules of the Association must be a fair commission under all the relevant circumstances. A broker also has the duty to get the best possible terms for his customers.

Rules Covering Brokers

The foregoing principles of the common law having to do with the obligations of a broker or agent to his customer or principal have found formal expression and amplification in certain of the Rules of Fair Practice of the Association and in certain of the so-called over-the-counter rules of the Securities and Exchange Commission, and, accordingly, to assure compliance with these formal requirements, every member (and all salesmen or employees who deal with the public) who acts as a broker for his customers should be thoroughly familiar with at least Article III, Sections 2, 3, 4, 12, 13, 14 and 15 of the Rules of Fair Practice of the Association and SEC Rules X-15C1-2, X-15C1-3, X-15C1-4, X-15C1-5, X-15C1-6 and X-15C1-7.

A Dealer's Duties

A member when acting as a dealer or principal in a transaction with a customer is acting essentially as a merchant, buying or selling securities for himself, for his own account, and, like all merchants, hoping to make a profit of the difference between the price at which he buys or has bought for himself and the price at which he sells for himself. A member when acting as a dealer or principal is thus not subject to the common law principles of agency which apply to a broker, but a dealer must at all times make it clear to his customer that he is acting as a dealer or principal, if that is the fact. He must be ever careful in such transactions not to make misrepresentations, directly or indirectly, with respect to the particular security being purchased or sold, and he must buy from or sell to his customer at a price which is fair, taking into consideration the market price, if any, market conditions, the expense involved, and all other relevant circumstances, and he should confirm to customers as dealer or principal.

Rules Covering Dealers

The foregoing principles with respect to the obligations of a dealer have also found formal expression and amplification in certain of the Rules of Fair Practice of the Association, in certain of the over-the-counter Rules of the Securities and Exchange Commission, and in certain sections of the Securities Act of 1933, so when acting as a dealer, a member (and all salesmen or employees who deal with the public) should constantly have in mind the provisions of Article III, Sections 2, 3, 4, 6, 12, 13, 14, 15 and 16 of the Rules of Fair Practice of the Association, and Rules X-15C1-2, X-15C1-3, X-15C1-4, X-15C1-5, X-15C1-6, X-15C1-7, and X-15C1-8 of the Securities and Exchange Commission, and Sections 12(2) and 17(a) of the Securities Act of 1933, as amended.

SUMNER T. PIKE

(Continued from Page 1)

Early Career Sketched

The following is a thumbnail sketch of Mr. Pike's earlier career:

Born: August 30, 1891, at Lubec, Maine. Education: Grade and high schools at Lubec; graduated Hebron Academy, Hebron, Maine; graduated Bowdoin College, Brunswick, Maine, class of 1913.


Army: 1917-19, various grades to Captain C. A. C. Principal duty, instructor in Officers Training Camp at Fort Monroe, Va.


Employment: 1920-22, vice president of Service Station Equipment Co. and Rupert Equipment Co., Dallas, Texas, and Kansas City, Mo.

Trading in Americas

Employment: 1923, Assistant to president of G. Amsinck and Co., New York City, engaged in trading with Central and South America.

Employment: 1924-28, American Fire Group of Fire Insurance Companies, New York City; employed in, and later in charge of, investment department.


Mr. Pike was appointed Business Adviser to the Secretary of Commerce on November 27, 1939.
TYPICAL COMPLAINTS:
HOW THEY ARE HANDLED
BY CONDUCT COMMITTEES

Two Cases Described—One Referred
to Association by Securities and
Exchange Commission

District Group Initiates Action

Editor’s Note: The presentation of
typical complaints and how they are
handled by District Business Conduct,
Committees is a regular feature of the
NASD NEWS.

Case No. 1

The SEC turned over to the Associa-
tion a complaint made to it by a cus-
tomer of a member charging (1) that
the member had recommended the sale
of a certain utility preferred stock, the
recommendation being based on “re-
ports of the Securities and Exchange
Commission,” that the customer sold
the stock on these recommendations at
66, and that the stock subsequently
topped par, and (2) that the member
sold certain bonds to the customer at
prices two to three points above the
prevailing asked price.

1. The District Business Conduct
Committee informally investigated and
found with respect to the first charge
that nearly a year had elapsed between
the sale of the stock and its reaching
par. The committee found further that
the dealer could not reasonably have
foreseen this rise and that the cus-
tomer had a 100 per cent profit in the
stock at the time of the sale. Further,
the committee noted that the customer
had told the member that he desired
to get into income producing securities
inasmuch as there were no dividends
being paid on the stock.

2. With respect to the second charge,
the member made available to the com-
mittee his confirmations on the other
side of all the transactions in question
and they indicated, in the opinion of
the committee, only a reasonable profit
and that the prices charged were not
out of line with prevailing prices. The
committee investigated the entire ac-
count and concluded that it appeared
to be “quite satisfactorily handled,”
that most of the items sold to the cus-
tomer showed a substantial advance,
and that the dealer had been meticu-
losus in sending proper confirmation, etc.

The Committee accordingly dismissed
the complaint and explained the trans-
actions to the customer, who expressed
change information and views with re-
spect to District administrative and le-
gal problems.

Francis A. Bonner, Chairman of the
Board of Governors, Joseph C. Hostel-
ter of Baker, Hostelier & Patterson,
General Counsel, and Wallace H. Ful-
ton, Executive Director, reviewed the
Association’s organization and activities
and discussed various administrative
and legal problems. Particular em-
phasis was placed upon the handling of
formal and informal complaints, quota-
tions on over-the-counter securities,
and the working out of uniform busi-
ness practices.

District Problems Discussed

District administrative and legal
problems were gone into in detail with
a view to standardizing administrative
procedure and perfecting liaison be-
tween Districts and between Districts
and the Washington office.

Those attending the meeting felt that
it would aid them greatly in their work
locally and that it would enable them
to serve their Committees and
the members in their respective Dis-

his satisfaction with the final disposi-
tion of the case.

Case No. 2

A District Business Conduct Com-
mittee charged a member with propos-
ing an exchange of bonds calculated to
yield excessive profits. The member
had sent a circular to holders of certain
real estate bonds suggesting a par for
par trade for certain utility bonds. The
circulated circular indicated that the real
estate bonds were due for difficulties and
that the utility bonds had good prospects
of appreciation. On the date the circula-
ted was sent out, the real estate bonds
were quoted about 10 points over the utility
bonds.

The member admitted that the profit
would have been excessive, but said
that he would not have allowed the
trade to be consummated under market
conditions as they existed at that time.
He also alleged that a subsequent letter
had been sent out offering a cash dif-
fERENCE on the trade.

The committee investigated and
found there had been no transactions in
the real estate bonds. The member
was requested to report any transactions he
had in the real estate bonds during the
next three months. The member had
no such transactions during that period
and the case was marked closed.

CLEVELAND MEETING
(Continued from Page 1)

SEC RELEASE
(Continued from Page 1)

of the actual price paid by him for the
securities, and in selling securities for
his customers, he credited them with an
amount far less than the actual price
received by him for the securities sold,
and in each case retained a secret profit
for his own use and benefit greatly in
ecess of the customary commissions;
that he purported to exchange cus-
tomers’ securities for other securities
having substantially an equivalent ag-
gregate market value, when in fact he
exchanged the customers’ securities for
other securities having at the time a
substantially smaller aggregate market
value.

Fraud Charged

“The complaint charged that the fore-
going acts, practices and course of busi-
ness operated as a fraud and deceit on
A’s customers.

“It further was alleged that A, in
the course of effecting transactions and
inducing purchases and sales obtained
money and property by means of un-
true statements of material facts.

“Among other things, the com-
plaint charged that the defendants B and C
previously had been associated with one of the
largest financial houses in New
York, that they were experts and
specialists in bonds and general se-
curities, and that customers might
have the utmost confidence in their
opinions and statements and could
deal with them in safety.

“The complaint alleged, how-
ever, that B and C had never been
associated with any financial house in
New York or elsewhere and prior to their association with A
had not had any experience in the
bond or general security business.

Position Not Disclosed

“The complaint alleged that A was
effecting transactions and inducing the
purchase and sale of securities by
means of other deceptive and fraudu-
 lent devices and contrivances in that he
failed to give or send to his customers
at or before the completion of each
transaction written notification disclosing
whether he was acting as a broker
for his customer, as a dealer for his
own account, as a broker for some
other person, or as a broker for the
customer and some other person.”

Note: In connection with paragraph
three of the above release, it should
perhaps be noted that it is unlawful
for an agent to make a secret profit,
whether such profit be large or small.
DISTRICT ACTIVITIES

COMMITTEE MEETINGS.
EDUCATION PROGRAMS.
OTHER EVENTS REVIEWED.

Chairmen Give Resumes of Work Carried on by Members in the Various Areas.

The NASD NEWS is inaugurating a new feature in this issue—“District Activities”—which will appear regularly in future issues. This feature, as its name implies, will be devoted to news and happenings in the various Districts with the thought of bringing all Districts into closer touch through the medium of the News.

District No. 1
From various sections of our District there have come evidences of a lively interest, on the part of Association members, in the NASD NEWS. Reports of the meetings and doings of the Board of Governors and of the several national committees are not only found to be of particular interest, but are serving to keep our membership, together, as a general understanding is had of the Association’s problems, purposes and accomplishments.

District No. 2
Our District is continuing in its efforts to carry on its campaign to educate the industry with regard to administration of our rules. It is our feeling that this campaign should be conducted by carrying our policy to the personnel of the various member firms, sales executives and sales forces through direct contact.

In recent weeks, our Uniform Practice Committee and Quotations Committee have been particularly active. At the present time we have only one unsettled case in the District, which is in Los Angeles.

District No. 3
The Denver newspapers began printing quotations on “Local Securities” on May 6 as the result of the excellent work of our Quotations Committee. This committee supervises the collecting, compiling, disseminating and publishing of these quotations. Several issues heretofore not quoted are now included in the list.

District No. 4
Our District Committee has not met since the last meeting of the Board of Governors of the Association in Washington, D.C., on April 29-30. We expect to hold a meeting very shortly.

We believe our membership is becoming more and more interested in the Association each month and at our forthcoming meeting we hope to appoint an Education Committee which will carry out this phase of our program in a more intensive way. Our Uniform Practice Committee expects to issue a bulletin shortly explaining some of the most misunderstood practices covered in the transaction of daily business.

District No. 7
The administrative machinery has been completely installed and is now operating with the District. With the addition of new members and the employees with the aims, objects and purposes of our Association, the Education Committee will hold meetings this month with executives and partners; cashiers and office managers; and salesmen and traders. These meetings should be very interesting and valuable to our members.

District No. 8
Recent activities in our District have included three meetings of the Full District Committee and meetings of the Quotations and Uniform Practice Committees. It was decided in March to initiate an educational campaign among the members and the Field Secretary, with the assistance of the District Chairman and Governors, to hold meetings in Omaha, Milwaukee, Grand Rapids, Detroit, Des Moines and Indianapolis.

The District Business Conduct Committee has been conducting informal complaint presented to it, concerning which hearings have not yet taken place, but are expected to be completed during June. The Quotations Committee also expects to complete its initial work in June and will, at that time, be prepared to offer its quotations for publication. The Uniform Practice Committee has appointed a subcommittee to draft suggestions for the national Uniform Practice Committee.

District No. 11
Since May 1 our District has handled four cases involving business conduct and the Business Conduct Committees in both Virginia and Maryland have done excellent work in running down the facts and thus bringing together complete information in each case. This has involved considerable work and time, but we feel that the results accomplished fully justify the effort. One case was brought by a member against another member and a settlement was arranged. Another case was brought by a customer against a member. In one case it was necessary to call in an outside accountant.

District No. 12
( eastern Division)

During the past several weeks there has been very little real activity in our District. The Quotations Committee has finally accomplished work on an agreement with the Philadelphia newspapers to include quotations furnished by the committee.

The Uniform Practice Committee held a meeting June 3rd for the purpose of drawing up a set of tentative rules which they felt would apply to this District in order that they may submit them to Joseph T. Johnson, chairman of the national committee.

District No. 13
Nevil Ford, Vice Chairman of the NASD, Harry W. Beebe, District Chairman, and Major Garnet C. Williams, District Committee, recently attended meetings in Buffalo, Rochester and Syracuse, and met with members with the activities and purposes of the Association.

At the meetings, Mr. Ford discussed the good relationship prevailing between the Association and the SEC, and assured members that all complaints and inquiries received equal attention. Mr. Williams summarized the activities of the Buffalo Business Conduct Committee of which he is the Chairman.

The Buffalo gathering on May 23 was arranged through the Buffalo Securities Dealers Association and its president, Frederick A. Terry of Schoellkopf, Hutton & Pomeroy, Inc., introduced the speakers. The Rochester meeting on May 24 was arranged by the Local Committee in that city composed of: Davis S. Rutt, Chairman; Walter H. Baumer; E. Harry Gilman; and John H. Kitchin. Edward J. Bullock, Chairman of the Syracuse Committee, arranged the meeting in that city which was held on the same day as the Rochester meeting.

In view of disturbed world conditions, the large turnout for these meetings was good evidence of the dealers’ interest in the Association.

Progress is being made by the special committee drafting uniform practice rules and it is expected that they will be presented to the full Uniform Practice Committee for approval in the near future.

District No. 14
Our District has no news of special import to report for the past month. Members of various committees have continued to study and investigate the problems assigned to them, and are looking forward with interest to the handing down of general policies from the various national committees.