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# Hurd Baruch, Wall Street: Security Risk

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# BOOK REVIEW

**WALL STREET: SECURITY RISK.** By Hurd Baruch. Washington: Acropolis Books Ltd. 1971. Pp. xii, 356. $8.95.

Business was booming on Wall Street in 1968. In fact, business had never been better. The average daily volume of shares traded on the New York Stock Exchange (hereinafter referred to as N.Y.S.E.) increased from 4.8 million in 1964 to nearly 13 million in 1968.[1] The Exchange set four new single-day volume records in 1968—the first time since October 29, 1929.[2] Approximately 24 million Americans were shareholders, with another 100 million persons participating indirectly through their interests in mutual funds.[3] To accommodate the increase in business, N.Y.S.E. member firms opened nearly 1,000 new branch offices in the same period (1964-68), bringing the total to 4,278.[4] Registered representatives, also known as account executives, increased in number by almost 17,000 to a total of 49,644.[5]

Business was so good in fact that brokerage firms were literally unable to handle it. Imagine General Motors closing down its plants one day each week in the middle of a record sales year—the business world would be dumbfounded! Yet, the N.Y.S.E. made a similar decision. Such drastic action is more easily understood when one realizes the serious problems that confronted the N.Y.S.E.

The securities industry was, and is, sales oriented. The primary aim of the broker is to find customers who want to sell or buy securities, from which transactions the firms make their commissions. Supporting the sales force is an institution known as the "back office." The back office staff of each firm is responsible for accomplishing the myriad tasks which accompany the purchase or sale of a security, *e.g.*, transfer, payment, delivery, extension of credit, hypothecation, and borrowing and lending securities. Traditionally, back office staffs have been the neglected stepsisters of the debonair broker. Partners of brokerage firms refused to direct their energies and cash to modernize and adequately staff the operations departments. Perhaps it was not so much direct refusal as ignorance of the need. In any event, the success of the sales force in 1968 crippled the back offices. Customers waited months in many cases for delivery of fully paid securities. Records of transactions were incomplete and in error. Complaints against broker-dealers to the

1. H. BARUCH, WALL STREET: SECURITY RISK 86 (1971) [hereinafter cited as BARUCH].
2. *Id.*
3. 34 SEC ANN. REP. xvii (1968).
4. BARUCH 89.
5. *Id.* at 88.

Securities and Exchange Commission increased startlingly from about 4,000 in 1968 to nearly 13,000 in 1969, ninety percent of which related to back office problems.[6] In an attempt to relieve pressure on the back offices, the decision was made to shorten daily trading hours and to close the Exchange one day each week.[7]

The back office backlog, however, was not the only problem. In March 1969, the long bear market began. Ultimately, the Dow Jones Industrial Averages fell from the all-time high of 968 in January 1969 to a low of 631 in May 1970.[8] For brokerage firms, the effect of this sustained decline in the value of stocks was not merely a slackening of business. The average daily volume in the summer of 1970, while less than in 1968, was still 7 to 8 million shares a day, well above its pre-1964 levels.[9] However, the decline in the value of securities in firm investment accounts and of customer securities used by the firms as collateral for loans, together with the loss of revenues from commissions, was the undoing of many firms with already frail capital structures.[10] On top of the still unresolved back office chaos of 1968, the results were disastrous. As a result of these pressures, over a hundred member firms of the N.Y.S.E. became defunct during 1969-70, and many more firms were perilously close behind. In addition, the accounts of hundreds of thousands of small investors were frozen for long periods of time.[11]

Is anyone responsible for such happenings? Can anything be done to prevent a reoccurrence? Hurd Baruch supplies an emphatic "yes" to both queries in *Wall Street: Security Risk*. Mr. Baruch, an S.E.C. lawyer, places the blame on the N.Y.S.E. for its failure to regulate its members adequately and sets forth specific recommendations for change. The seriousness of his indictment of the N.Y.S.E. and the scope of his recommendations demand analysis.

For those unfamiliar with the Congressional scheme for the regulation of the securities industry, a few words are in order. In an effort to insure free and honest securities markets following the stock market crash of 1929, Congress enacted six major pieces of legislation relating to the securities industry and established the S.E.C. to administer the Acts.[12] The Securities Exchange Act of 1934[13] is the Act most relevant

6. 35 SEC ANN. REP. 2 (1969).
7. 34 SEC ANN. REP. 16 (1968).
8. BARUCH 145.
9. *Id.*
10. *Id.* at 149.
11. *Id.* at 15.
12. The six acts administered by the S.E.C. are: (1) Securities Act of 1933 (15

to an analysis of Baruch's book. Among other things, the Exchange Act provides for the registration of broker-dealers with the S.E.C.,[14] requires the registration of national securities exchanges with the S.E.C.,[15] prohibits various activities of broker-dealers, including market manipulation[16] and fraud in the purchase or sale of securities,[17] sets forth certain ground rules for the operation of a brokerage business for the protection of investors,[18] and empowers the S.E.C. to promulgate rules and regulations in the public interest. An important element in this particular legislative scheme is the provision for self-regulation of registered exchanges. Thus, the N.Y.S.E., by registering with the S.E.C., became obligated to establish rules for its members designed to protect investors and to enforce compliance with its own rules, as well as the rules of the S.E.C.[19] Thus, the N.Y.S.E. has the primary duty to enforce the securities laws, while the S.E.C. retains residual power. It is within the context of this legislative scheme that Baruch indicts the N.Y.S.E. as being primarily responsible for the failure to police brokerage firms adequately, thereby contributing substantially to the chaos of 1968-70. Baruch does not find the same fault with the S.E.C., claiming that the Commission knew what was happening but was powerless to act directly.

It should be made clear at this point that the Commission's regulatory powers, although residual, provide some methods for controlling the N.Y.S.E. and its members. Section 19(b) of the Exchange Act specifically empowers the S.E.C. "by rule or order" to "alter" or "supplement" rules of the N.Y.S.E. for the protection of investors or in the public interest. Further, Section 19(a) of the Exchange Act empowers the S.E.C. to suspend or withdraw completely the registration of the Exchange for failure to enforce compliance with the S.E.C.'s rules. That the S.E.C. has been hesitant to use such powers is perhaps politically understandable. Nevertheless, if by hindsight we are able to isolate

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U.S.C. §§ 77a-77aa), (2) Securities Exchange Act of 1934 (15 U.S.C. §§ 78a-78jj), (3) Public Utility Holding Company Act of 1935 (15 U.S.C. §§ 79a-70z), (4) Trust Indenture Act of 1939 (15 U.S.C. §§ 77aaa-77bbb), (5) Investment Company Act of 1940 (15 U.S.C. § 80a) and (6) Investment Advisers Act of 1940 (15 U.S.C. § 80b). In addition, the Commission has advisory responsibilities under the Bankruptcy Act, Chapter X (11 U.S.C. ch. 10).

13. 15 U.S.C. §§ 78a-78jj (1934), *as amended*, 1964, 1970 [hereinafter cited and referred to as Exchange Act].

14. Exchange Act § 15.

15. *Id.* § 6.

16. *Id.* § 9.

17. *Id.* § 10(b).

18. *E.g., Id.* § 8(b).

19. *Id.* § 6(a)(1).

instances wherein the N.Y.S.E. failed to regulate its members adequately, the S.E.C. cannot be characterized as having been either powerless or blameless.

Baruch describes ten failures of the N.Y.S.E. in the 1968-70 era.[20] As his complaints are reviewed below, it should be noted that there are areas of substantial agreement between this reviewer and Baruch. However, this reviewer disagrees with Baruch's contentions that the S.E.C. is blameless and that the N.Y.S.E. is completely negligent. An accurate appraisal of the crisis on Wall Street in 1968-70 must put the role of the S.E.C. in perspective.

(1) *The N.Y.S.E. and its member firms failed to plan adequately for the increasing business of 1968, thereby causing the back office chaos.* Brokerage firms could not handle the paperwork caused by a rapidly increasing volume of business in 1968. Ironically, a study commissioned by the N.Y.S.E. in the mid-1960's had projected daily volume on the N.Y.S.E. to double by 1975 to about 7.6 million shares.[21] In fact, as noted earlier, the volume more than tripled by 1968, to nearly 13 million shares per day. Clearly, the study itself is evidence that the Exchange was engaged in some planning, but more significantly, that nobody (including the S.E.C.) suspected the degree to which business would in fact grow. Nevertheless, it is clear that brokerage firms traditionally have neglected the back offices. Wall Street—the symbol of American business—is, in reality, its most poorly managed branch. Back offices have been understaffed and their workers underpayed and undertrained. Wall Street has been too slow to take advantage of the computer to streamline its complicated paperwork operations.[22] While law has often motivated management reform, it undoubtedly failed in the case of securities management from 1964 to 1968. The S.E.C., after the paperwork crunch was upon back office staffs, did, however, notify the industry that it would consider it a violation of the anti-fraud provisions of the Exchange Act for firms to accept orders if they were not able to deliver cash and securities to customers promptly.[23] This move by the S.E.C. was an admission of its power to act; however, it was also a demonstration that the S.E.C., as well as the N.Y.S.E., acted too little and too late to be effective.

20. Baruch summarizes the ten N.Y.S.E. failures in Chapter 16, the last. His book in general presents arguments in support of the ten complaints.

21. 35 SEC ANN. REP. 1 (1969).

22. BARUCH ch. 5.

23. SEC Securities Act Release No. 8363 (July 29, 1968).

(2) *The Exchange failed to implement a consistent and effective program for imposing restrictions on firms undergoing operational strains.* Baruch contends that, had the Exchange adequately inspected its member firms, it would have known the problems being caused by the paperwork jam. Furthermore, the N.Y.S.E. was ineffective even in those cases in which it had knowledge of the problems.[24] In this context, it is instructive to note that the S.E.C., with the power to inspect books and records of broker-dealers, actually conducted fewer investigations during the crisis of 1968 (514)[25] than it had in 1966 (1,272).[26] This decline in the number of investigations was caused in part by financial restraints upon the Commission, necessitating a change from regular inspections to surprise inspections. However, if the S.E.C. knew that the N.Y.S.E.'s enforcement methods were ineffective and that the protection of investors was at stake, why did it not act? As noted above, not only has the S.E.C. power to demand enforcement of both Commission and Exchange rules by the N.Y.S.E.,[27] but also the power to "alter" or "supplement" inadequate Exchange rules, including safeguards regarding financial responsibility,[28] hours of trading,[29] time and method of settling transactions and delivery,[30] and "similar matters."[31]

A further element in Baruch's second complaint is that whatever the restrictions upon Exchange members were, they were not applied consistently by the N.Y.S.E. That is, "old line" members of the Exchange constituted a "club," the members of which were treated more favorably than newcomers.[32] This complaint is no doubt true. Robert W. Haack, President of the N.Y.S.E., who receives a good deal of criticism from Baruch, has been, interestingly, Wall Street's most vocal opponent of "clubbiness" in the Exchange.[33] But has the S.E.C. altogether avoided the same preferential treatment of club members? Take, for example, the S.E.C. action against Lehman Bros., an old line member of the Exchange.[24]

In August 1968, the Commission began administrative proceedings

24. BARUCH ch. 6.
25. 34 SEC ANN. REP. 96 (1968).
26. 32 SEC ANN. REP. 62 (1966).
27. Exchange Act § 19(a).
28. *Id.* § 19(b)(1).
29. *Id.* § 19(b)(4).
30. *Id.* § 19(b)(7).
31. *Id.* § 19(b)(13).
32. BARUCH ch. 13.
33. *E.g.*, Address by Robert W. Haack to Economic Club of New York, November 17, 1970, quoted in Wall Street Journal, November 18, 1970, at 3.
34. *See* BARUCH 105-11 for his account of the S.E.C.'s action.

against the firm for failing to make accurate and keep current certain books and records in accordance with the federal securities laws. One may first wonder why the Commission did not act against all firms regulated inadequately by the Exchange, since the action against Lehman Bros. was an admission of such power. Nevertheless, let us examine the Lehman Bros. case in the light of Baruch's charge of club preference by the N.Y.S.E. At first glance, the Commission's actions against Lehman Bros. seem to support Baruch's contention that the S.E.C. plays no favorites. However, the S.E.C. could have suspended or revoked the firm's registration; in fact, it did neither. Baruch terms the Commission's action as "spectacularly successful," because,

> [i]n return for dropping the suspension issue, the Commission got various commitments from the firm, chiefly that it would resolve its remaining deficiencies in accordance with a specific program and that it would hold transactions down.[35]

Additionally, the S.E.C. dropped allegations against the managing partner because the final order of the Commission censured all general partners. In other words, the Commission's "tougher" enforcement policy amounted merely to a slap on the wrist and a request for a promise to clean up the mess.

Obviously, the exercise of enforcement discretion is a complicated matter. However, both the N.Y.S.E. and the S.E.C. seem to take a softer line against members of the club and both must share the blame for the resulting perversion of the public interest.

(3) *The N.Y.S.E. did not act to "choke off the tremendous surge of volume" in Exchange business.*

Baruch's argument is that, had the N.Y.S.E. acted to ban advertisements, curtail the hiring of registered representatives and restrict the opening of new offices, member firms would have done less business, thereby alleviating the back office problem.[36] One might first question whether the N.Y.S.E. ought to have the power to prohibit advertising or to limit the public's access to the securities markets by purposely limiting the number of offices and sales personnel. Even if it is assumed that the Exchange should have such power, Baruch's allegation that the Exchange did not act to restrict business seems somewhat inaccurate.

In June 1968, the Exchange requested member firms, especially those with severe back office problems, to reduce advertising and pro-

35. BARUCH 108-09.
36. *Id.* at 136.

motion, to cease solicitation of over-the-counter transactions, to reduce or discontinue firm trading, to disallow commission credit on securities selling at less than $5, $7, or $10, and to terminate registered representatives who did not strictly observe industry and firm policies.[37] Although these measures were too little and too late, they do manifest at least some form of action by the Exchange.

Meanwhile, the S.E.C., though possessing the power to alleviate market pressures, did little more than issue halfhearted threats. In July 1968, the S.E.C. warned brokers that:

> Broker-dealers who are unable to consummate all their securities transactions promptly in accordance with traditional customs and usage of trade, or who are encountering any delays because of back-office problems of any kind, are compounding their difficulties and increasing the likelihood of disciplinary action being taken against them if during any such period they advertise, employ additional salesmen, or take any other action designed to expand the volume of their businesses.[38]

This policy statement was an admission of S.E.C. power and, in view of its timing, as belated as the N.Y.S.E.'s own action. More important, the S.E.C. failed to follow up its policy statement with action.

(4) *After the trading volume dropped in 1969, the N.Y.S.E. did not require members to "clean up the paperwork blizzard."* Mr. Baruch's criticism is quite accurate. However, it should also be pointed out that the S.E.C. similarly failed to use its power to demand that the Exchange enforce compliance with both Exchange and Commission rules.

(5) *The Exchange misinformed Congress and the public about the financial crisis during 1969-70.* If Baruch is suggesting a willful design to misinform Congress, such a charge is, of course, serious. However, it is more likely that Baruch is merely criticizing the Exchange for its faulty analysis of the severity of the crisis. Whichever is the case, it is obvious that the S.E.C., in its official messages to Congress during those years, issued misleading statements. In the 1968 annual report of the Commission, the S.E.C. announced that it was "actively oversee[ing]" the Exchange.[39] The S.E.C. further admitted that it had the power to change the rules of the Exchange to protect investors,[40] but omitted to

37. *Id.* at 130.
38. SEC Securities Act Release No. 8363 (July 29, 1968).
39. 34 SEC ANN. REP. 67 (1968).
40. *Id.* at 62.

state that it had not used that power in spite of the need. Out of a total of 192 pages, only one and one-half were devoted to a description of " 'Back Office' Problems,"[41] which problems, the report conceded, had resulted from the "unforeseen level of volume" in trading. The report went on to say that the Commission

> has stressed the responsibility of individual firms and the self-regulatory agencies to deal with these problems and has *encouraged* them to take all necessary measures. . . . *Where violations have been found, appropriate enforcement action has been taken.*[42]

The Commission's description of the back office problem failed to disclose that the S.E.C. had abstained from using the full extent of its power to protect investors. At best, its description of the back office problem was understated.

(6) *The N.Y.S.E. failed to protect adequately customers' funds and securities used in the operation of the brokerage business.* Perhaps to the surprise of many readers, brokerage firms exist on terribly fragile capital structures. Working capital to carry on the firms' operations is dependent, to a large extent, on the use of customers' funds and securities on deposit. In fact, as Baruch points out, equity capital supplied by the owners of brokerage firms usually amounts to a good deal less than the funds available for use from customers,[43] leading Baruch to observe: "What is unique about the stock market is that the amateur players in the market stake the professionals with the cash and securities they need for playing the game!"[44]

Customers' funds used in the operation of the business are available directly from free credit balances and indirectly from the use of customers' securities. Free credit balances represent customers' cash on deposit with brokers, the cash representing the proceeds of a sale or cash having been deposited prior to an order to purchase. In any event, the funds, which are substantial, are available for use by the firms. Baruch estimates the aggregate amount available to all N.Y.S.E. firms in recent years as varying between 2 and 3.7 billion dollars.[45] According to Baruch, firms can earn about 262.5 million dollars annual profit from the use of these funds (assuming free credit balances of 3 billion dollars and an 8.75% interest rate).[46]

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41. *Id.* at 16-17.
42. *Id.* (emphasis added).
43. BARUCH ch. 1.
44. *Id.* at 18 (emphasis added).
45. *Id.* at 21.
46. *Id.* at 25.

Customers' securities on deposit with firms include fully paid securities left for safekeeping, as well as securities purchased on credit (margin). Such securities are used by firms (1) for hypothecation (pledged as collateral on loans), (2) for lending to other firms (for which 100% cash deposits are received, which deposits can be used), and (3) for delivery to other customers or brokers to cover purchases for which the firm does not have securities on hand. Section 8(c) of the Exchange Act prohibits firms from commingling customers' securities with securities under a lien unless the customers consent in writing. The same section also prohibits the hypothecation of customers' securities in an amount exceeding the aggregate indebtedness of all customers to the firm. Section 8(d) of the Exchange Act prohibits the lending of customers' securities without their written consent. When viewed realistically, however, the requirement of consent affords little protection to the customer. As Baruch points out, all customers "agree" to the commingling and lending of their securities when they open their accounts.[47] Furthermore, in times of financial crisis, the temptation to pledge securities on loans over and above the aggregate indebtedness of all customers is great. Nevertheless, the rules, such as they are, could have been enforced by the Commission. According to the S.E.C.'s 1969 annual report, however, its program of surprise inspections of 732 broker-dealers turned up only four instances of improper hypothecation.[48]

Baruch recommends rules that would require brokerage firms to establish cash reserves against the amount of customers' securities and funds used in the operation of the business, and limit the use of customers' funds and securities to the financing of margin accounts.[49] If the S.E.C. lacked power in the past to promulgate such rules, Congress has now mandated such action in a 1970 amendment to Section 15 of the Exchange Act. The amendment gives the Commission power to make rules

> for the protection of investors to provide safeguards with respect to the financial responsibility and related practices of broker-dealers including, but not limited to, the acceptance of custody and use of customers' securities, and the carrying and use of customers' deposits or credit balances. *Such rules and regulations shall require the maintenance of reserves.*[50]

47. *Id.* at 54.
48. 35 SEC ANN. REP. 88 (1969).
49. BARUCH 250-65.
50. Exchange Act § 15(c)(3), *as amended* December 30, 1970 (emphasis added).

The ball is now in the Commission's hands.[51]

(7) *The Exchange refused to take adequate steps to insure the liquidity of member firms.* Both the S.E.C.[52] and the N.Y.S.E.[53] have so-called net capital rules. These rules are designed to insure liquidity of brokerage firms against the obvious hazards resulting from exposure of customer cash and securities on deposit to loss. In the most simple terms, the present S.E.C. and the N.Y.S.E. rules are similar: a firm's aggregate indebtedness may not exceed 2000 *per centum* (20:1 ratio) of its net capital. The catch, of course, is in defining those terms to be included in arriving at net capital and aggregate indebtedness. During the crisis of 1968-70, the N.Y.S.E. interpretation was more lenient, thus permitting firms to continue operating under conditions which would not have been tolerated under the S.E.C.'s interpretation.[54] Baruch bemoans the fact that the N.Y.S.E. rule prevailed. At this point the facts should be consulted in an attempt to understand the circumstances under which the N.Y.S.E. rule prevailed.

The Exchange Act provides in Section 8(b) for the net capital rule to be applied to N.Y.S.E. firms according to such rules as the S.E.C. may prescribe. The S.E.C., however, never prescribed any such rule. The Commission did promulgate a net capital rule pursuant to another section of the Exchange Act (§ 15(c)(3)),[55] but *exempted* the N.Y.S.E. from its coverage. It was provided, however, that the exemption could be withdrawn on ten days notice if the "protection of investors" warranted.[56] First, it must be noted that the S.E.C. was not required to exempt the Exchange. Second, it is clear that the S.E.C. retained the ultimate power to remove the exemption. Therefore, to the extent that the N.Y.S.E. rule worked to the detriment of investors (as it clearly did), the S.E.C. could have made a more stringent rule applicable. Not having done so, the Commission must share the blame for the adverse consequences.

(8) *The N.Y.S.E. refused to take enforcement action in some cases and sometimes blocked Commission action.* As mentioned previously, Section 19(a) of the Exchange Act empowers the S.E.C. to proceed against the Exchange for failing to enforce compliance with its

51. The S.E.C. has proposed Rule 15(c)(3-3) (not yet effective) which would require cash reserves and limit the use of customers' funds. *See* SEC Securities Act Release No. 9622 (June 4, 1972).

52. 17 C.F.R. § 240.15c3-1 (1970).

53. N.Y.S.E. CONSTITUTION AND BY-LAWS Rule 325.

54. *See* BARUCH 177-88 for an analysis of the weaknesses of the N.Y.S.E. rule.

55. 17 C.F.R. § 240.15c3-1 (1970).

56. *Id.* § 240.15c3-1(b)(2).

rules or the federal securities laws. Further, as already noted, the Commission, by its own admission, had the power to enforce the securities laws directly against member firms. In this same context, Baruch is critical of the Exchange's use of its Special Trust Fund, established to protect customers of insolvent member firms. The fact remains, however, that the N.Y.S.E., through its members, will have provided, according to Baruch's own estimate, approximately 125 million dollars to protect customers of member firms.[57] The S.E.C., through no fault of its own, is powerless to recover a single cent for such investors. Hopefully, the Securities Investor Protection Act of 1970 will partially fill this need by insuring customer accounts up to $50,000.[58]

(9) *The N.Y.S.E. did not take advantage of technological possibilities to improve the industry's operation.* Baruch criticizes the Exchange both for its failure to make better use of the computer in transacting business and for its failure to move toward a "certificateless" operation.[59] This reviewer is in complete accord with such criticism. The use of negotiable stock certificates, which must be hand-delivered, held for safekeeping and re-issued in the names of new owners, causes untold delay and congestion in the back office. The elimination of stock certificates and the use of computers to record sales, amount and ownership would relieve the paperwork backlog in the back offices and decrease expenses (Baruch estimates a cost reduction of one-third).[60]

(10) *The N.Y.S.E. refused to give up its monopolistic fixed-commission rate scheme.* The member firms of the N.Y.S.E. operate under a minimum fixed-commission structure. Baruch, among others, urges that commissions be negotiated.[61] While Baruch singles out the Exchange as being responsible for the failure to change, it must be noted that the S.E.C. has the power, pursuant to Section 19(b) of the Exchange Act, to "alter" or "supplement" Exchange rules dealing with the fixing of reasonable rates.[62] Only after significant pressure from the Department of Justice in early 1969[63] did the Commission begin to re-evaluate fixed commissions seriously. Even then, the S.E.C. did not finally work out a plan by which commissions on orders exceeding

57. BARUCH 307-08.
58. Pub. L. No. 91-598 (December 30, 1970).
59. BARUCH 279-86.
60. *Id.* at 282.
61. *Id.* at 291-97.
62. Exchange Act § 19(b)(9).
63. Memorandum of the U.S. Department of Justice on the Fixed Minimum Rate Structure at 193-95, submitted at S.E.C. Rate Structure Hearings (January 1969).

$500,000 could be negotiated until early 1971.[64] The question of negotiated *versus* fixed commissions is not a simple matter. While Baruch cites Merrill Lynch, Pierce, Fenner & Smith, Inc., the nation's largest firm, as favoring negotiated commissions,[65] it should be noted that Merrill Lynch is precisely the kind of firm that would benefit by such a change because of the tremendous volume of their business. Small trades (odd-lots and 100 or 200 share lots) are not profitable unless volume is large. Thus, with smaller, negotiated commissions, small firms would be unable to compete with larger firms like Merrill Lynch. While Baruch advises a healthy dose of competition for Wall Street,[66] he admits that freely negotiated commissions might result in the creation of only "several dozen large regional and nationwide firms."[67] However, there appears to be no reason why commissions on large institutional orders ought not to be freely negotiated in view of the high margin of profit. The present scheme by which trades over $500,000 can be negotiated is a step in the right direction, but the limit ought to be much lower.

This review of Baruch's ten major complaints against the N.Y.S.E. is not intended, on the whole, as an expression of complete disagreement. If, however, the regulatory failures of 1969-70 are to be described and evaluated accurately, the S.E.C. must share criticism with the N.Y.S.E. While it is true that, under the legislative scheme, the N.Y.S.E. is granted the power to regulate itself, it is also true that the S.E.C. was not, and is not, powerless to intervene.

Baruch's argument, of course, is that self-regulation has been a failure and consequently all, or at least more, power must reside in the Commission.[68] It is not clear, however, that the Commission has made full use of the power it now commands. This reviewer does not agree with Baruch that "(c)ertainly, it is clear that the Commission has not been and is not now captive of the industry it regulates."[69] By failing to correct inadequate Exchange rules, by failing to enforce the federal securities laws fully and by failing to use available legal means to discipline the Exchange for not regulating its members adequately, the S.E.C. seems to have breached its statutory duty to protect investors.

In no small way, perhaps, is this due to a ridiculously low budget.

64. SEC Securities Act Release No. 9079 (February 11, 1971).
65. BARUCH 293.
66. *Id.* at xii.
67. *Id.* at 297.
68. Baruch generally argues against self-regulation. *But see* BARUCH 299.
69. BARUCH 312.

In 1970, for instance, the S.E.C. budget was a mere 21.9 million dollars, as compared to the N.Y.S.E. budget of 69 million.[70] More important, the actual cost to taxpayers to support the Commission was only 6.4 million dollars, inasmuch as fees paid to the S.E.C. annually provide the majority of the budget. If Baruch's book does no more than motivate Congress to allocate more realistic funds to the S.E.C., it will be a success.

Baruch's efforts are most significant in that they present an analysis of that hitherto ignored institution—the back office. However, if essential changes are to be made in the regulation of the securities industry, the failures of the S.E.C., as well as the N.Y.S.E., must not be ignored.

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70. *Id.* at 313.

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