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BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

Docket No. _____

In the matter of JAPANESE AMERICAN DEPOSITORY

CONFERENCE

Place Washington, D.C.

Date June 28, 1961

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EDDSON:

BEFORE THE

SECURITIES AND EXCHANGE COMMISSION

In the matter of:

JAPANESE-AMERICAN DEPOSITORY

Conference

Room 292, Securities and Exchange
Commission Building
425 Second Street, N. W.
Washington, D. C.
June 28, 1961

The conference was held, pursuant to notice, at
10:00 o'clock a.m.

EXPOS:

MANUEL F. COHEN, Division of Corporation Finance;
PHILIP A. LCOMBS, JR., Division of Trading and Ex-
changes; and
EUGENE H. ROYBEE, Division of Corporation Finance,
Securities and Exchange Commission.

APPEARANCES:

JAMES A. AUSTIN, Irving Trust Co., 1 Wall Street,
New York 15, New York, appearing on behalf of Irving Trust Co.

GEORGE A. BROWNELL, of Davis, Falk, Waribell, Sander-
land & Kindle, 15 Broad Street, New York City, appearing on
behalf of Morgan Guaranty Trust Company of New York.

LAURENCE L. CARTER, Irving Trust Company, 1 Wall
Street, New York 15, New York, appearing on behalf of Irving
Trust Co.

APPEARANCES (Continued):

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✓ JOSEPH A. DOYLE, of Sherman and Sterling, 20 Exchange Place, New York City, appearing on behalf of The First National City Bank of New York.

✓ W. D. CARR and ALBERT DOYLE, New York City, appearing on behalf of the Chemical Bank New York Trust Company.

✓ HOWARD EISEN, National Association of Securities Dealers, Inc., 25 Broad Street, New York City, appearing on behalf of the Foreign Securities Committee of the NASD.

✓ HENRI L. FROY, Abraham & Co., 120 Broadway, New York City, appearing on behalf of the Foreign Securities Committee of the National Association of Securities Dealers, Inc.

✓ DEWICK GREENCOCK, of Carl M. Loeb, Rhodes & Co., 42 Wall Street, New York City, appearing on behalf of the Foreign Securities Committee of the National Association of Securities Dealers.

✓ R. E. MOHLEY, 140 Broadway, New York City, appearing on behalf of the Morgan Guaranty Trust Company.

✓ JAMES E. ROBERTSON, Vice President, The First National City Bank of New York, 2 Broadway, New York City, appearing on behalf of The First National City Bank of New York.

✓ W. J. SCHERER, New York City, appearing on behalf of the Chemical Bank New York Trust Company.

✓ EDWIN P. STEVENS, of Winthrop, Stinson, Pataen & Roberts, 40 Wall Street, New York City 5, appearing on behalf of the Irving Trust Company.

1 APPEARANCES (Continued):

2 J. E. STEVENSON, of Sullivan & Crowell, New York
3 City, invited as counsel for underwriter in Sony Financing.

4 GEORGE E. REEBER, 25 Broad Street, New York City 4,
5 appearing on behalf of the Foreign Securities Committee of
6 the National Association of Securities Dealers.

7 EDWARD TRAVERS, Vice President, Manufacturers
8 Trust Company, New York City, appearing on behalf of the
9 Manufacturers Trust Company.
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PROCEEDINGS

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MR. COHEN: Good morning, gentlemen. I want to apologize for being late. I was in the Chairman's office. I didn't realize when I ran past the ten o'clock hour.

First let me say I hope we are all here. We are interested in this ADR problem for the Japanese securities.

Just so that we get started without further ado, there were four problems -- maybe there were three, but I have then listed as four -- that I thought would permit some discussion today. Of course the first question is the registration of ADR's for Japanese securities, particularly the ones as to which registration statements have already become effective.

Second -- and this may be part of the first -- the nature of the disclosure in addition to that specifically required by Form S-12 by reason of the particular problems that we have discussed or encountered in connection with Japanese securities. I have in mind not only currency restrictions, but particularly problems which may arise from the practice of Japanese companies in financing the operations of such companies.

More specifically, as I understand it, many Japanese companies engage in a procedure whereby they make rights offerings, or that are akin to rights offerings, on a frequent basis, and at a price which may result in dilution to

1 investors of a substantial character unless these investors
2 either have an opportunity to avail themselves of the rights
3 offering or to dispose of the rights in a manner that is
4 possible in this country so as to realize the equivalent or
5 nearly the equivalent.

6
7 The third point relates to a problem that exists
8 or arises, or perhaps is imaginary, in the area of those ADR's
9 which have been issued by different banks and relating to
10 the same security -- that is, the duplication of ADR's.

11 Finally, I have listed on my notes here a general
12 question which harkens back to the time when Form S-12 was
13 originally adopted, and that relates to the question of whether
14 or not Form S-12 has been used since its adoption and whether
15 it is proposed to be used in connection with Japanese securi-
16 ties to accomplish a purpose not intended by the Commission
17 when it adopted Form S-12.

18
19 More specifically, I have in mind that at the time
20 of the adoption of that form it was urged upon the Commission
21 that Form S-12 was sought by the trading community, and the
22 banks were willing to accommodate the trading community in
23 this area to assist in dealing with or obviating certain
24 mechanical problems that arise in trading securities of foreign
25 origin; that neither the trading community nor the banks
sought Form S-12 or some solution of the problem as it was
then presented to provide a means for introducing into

1 the American market securities which had not theretofore
2 enjoyed a trading market.

3 There has been some concern expressed in the Com-
4 mission that Form S-12 has been or may be proposed to be a
5 means of achieving a result not intended by Form S-12. That
6 is my point No. 4.

7 Perhaps it would be best to start with point No. 4,
8 because if there is a major problem in point No. 4 with regard
9 to the Japanese ADR's, that might resolve all the other prob-
10 lems. I would like to get an expression of view from the
11 bankers as well as an expression of view from those here who
12 perhaps can be described more accurately as representing the
13 trading community.

14 Just as a matter of convenience, I will start with
15 Mr. Brownell, since Mr. Brownell has a long and intimate asso-
16 ciation with problems of ADR's.

17 MR. BROWNELL: Mr. Cohen, let me first say that
18 Morgan Guaranty Trust Company of New York, whom I represent,
19 and the other banks who I am sure will introduce themselves
20 in due course -- and I am sure also the others here -- appre-
21 ciate very much the opportunity to discuss these four ques-
22 tions with you.

23 I will say for the record, as you know, this confer-
24 ence is an outgrowth of a previous conference held some weeks
25 ago in your office. At that time the four banks here present

1 had filed Form S-12's with respect to the stocks of some twenty
2 Japanese companies. There were certain overlaps among those
3 filings so that in four or five of the cases there were two
4 registration statements applicable to the stock of one com-
5 pany.

6 Some of those registration statements became
7 effective. I understand in other cases, delaying amendments
8 were filed and three did not become effective. And apparently
9 questions were raised, either within or without the SEC,
10 which led you to call a meeting which was attended and at which
11 the entire subjects -- not all of the subjects that you have
12 mentioned, but several of them -- were discussed.

13 You decided, with the concurrence of the banks
14 present, that there should be further examination of some
15 of those questions by all concerned; and you indicated at
16 that time that in due course you would call a further con-
17 ference and we would discuss the matter further.

18 I imagine that one of the purposes for this con-
19 ference is to carry out that general understanding at that time.

20 You asked that we turn first to the fourth question.
21 My mind goes back to the days in 1955 when the full Commis-
22 sion held a hearing on the general subject of ADR's. It
23 is not necessary for me to review what took place at that
24 time because there was a written record, and it is set forth
25 in the minutes of that meeting of January 20, 1955.

1 But at that time there were present not only, I
2 believe, all the banks now present and others besides; but
3 representatives of various trading firms and I believe others.
4 One of the things that the full Commission gave attention to
5 at that time, I am sure, was the entire question of the
6 usefulness and the desirability of ADR's being made avail-
7 able on a broader scale than had been possible up until that
8 time.

9 We argued that ADR's could be issued freely by
10 banks under the 3(a)(2) exemption in the 1933 Act on the
11 theory that the ADR's themselves were securities issued by a
12 bank. That, of course, would have greatly facilitated the
13 use of the ADR's.

14 The Commission decided not to accept that prin-
15 ciple, and in so doing being consistent with a position
16 previously taken by it.

17 But after the hearings, the Commission issued
18 Form S-12, which made it possible for banks to file regis-
19 tration statements with respect to ADR's covering foreign
20 securities without having the bank itself designated as the
21 issuer of the securities, and with much more limited dis-
22 closures than would be necessary in that event applicable to
23 the bank; and without disclosures applicable to the underlying
24 securities -- it being, of course, understood that the form
25 was not to be made available for use in connection with the

1 issuance of ADR's for new offerings of securities.

2 I recently re-read the minutes of that meeting of
3 June 20, 1955. I am also mindful of the conferences that
4 were held by numbers of those present afterwards, of
5 which no stenographic record was kept. I know that, at
6 those meetings, the Commission was very much interested in
7 being sure that ADR's were not used as a cloak or means of
8 introducing new issues of securities into the United States
9 which would normally have to be registered.

10 In other words, to use the lingo in the trade, the
11 ADR's were not to be issued against "hot stock."

12 I do not find in the minutes of the June 20 meet-
13 ing, nor do I recall in our subsequent conferences, any ex-
14 tended expression of views by the Commission that ADR's
15 were not to be used to make available to the American market
16 simplified means of dealing in securities of foreign issuers
17 which previously had not been broadly dealt in in the American
18 market

19 However, you asked for an indication of the procedure
20 that has been followed by the several banks in connection
21 with ADR's up until this time, and that I am glad to give to
22 you -- subject to correction by Mr. Moxley of Morgan Guaranty
23 Trust Company, who is here with me.

24 It has not been the practice of Morgan Guaranty
25 Trust Company of New York in any case to file an S-12 covering

the issue of ADR's for the purpose of bringing into the American market stocks of companies not previously held in the American market and not previously traded in in the American market.

The usual situation involves a case where there has been to a considerable extent foreign holdings of a certain security in the United States. Before going forward with an S-12, Morgan Guaranty satisfies itself of that fact.

Morgan Guaranty also does make inquiries in the market as to the extent of the interest in those securities, and in some cases it may find that the difficulties of trading in the security are so great that the extent of the American participation would not be as great as it would be if ADR's were made available for the issuer.

That factor of additional interest is, of course, one taken into consideration when the bank decides whether or not to file an S-12. The bank takes great precautions to insure that they do not put out a new issue of ADR's either for the purpose of enabling brokers, dealers, foreign issuers, underwriters, or others to distribute in this market shares of stock that would normally have to be registered. We know that the form is not applicable in a case of that kind.

As a matter of fact, the law would involve serious difficulties in a case of that kind. It is not necessary for me here to outline the precautions that we take -- although

if you wish at a later time in the hearing I shall be glad to do so.

The ADR machinery which was devised by the Commission and those working with it in 1955 has, I believe, worked satisfactorily. I do not know exactly how many securities are now covered by ADR's, but I think the number is somewhere in the neighborhood of 150 -- maybe more. Some of those issues, of course, antedate the 1953 Act. They aren't all S-12's and I don't know exactly how many of them are S-12's.

Of those 150, Morgan Guaranty Trust Company of New York is the depository for approximately 94. Of those 94, I believe something in the neighborhood of fourteen or fifteen represent issues where other banks also act as depositaries for foreign stocks. In other words, cases where there is a duplication that you referred to in your third point.

We will doubtless have more to say on that later on. But I must at the outset say in passing that, having lived with the subject as counsel for the bank in this matter, I have never yet found any difficult to arise from the fact that such duplications exist.

That, Mr. Cohen, is a general statement about our policy and attitude. Maybe you would want to ask questions after you have gotten the opinions of others. I will be glad to try and answer them when that time comes.

1 MR. COHEN: I would like to stay with that one
2 point for the moment. Just by way of response to what you
3 have said, it is true that the form and the main burden of
4 the discussion in 1955 with respect to the securities prob-
5 lem stemmed from a concern whether or not the ADR could,
6 unwittingly or otherwise, be used as a procedure to introduce
7 into the American market securities which should be regis-
8 tered -- securities stemming from someone acting as an under-
9 writer for an issuer or someone who might have a control re-
10 lationship with an issuer. This was, of course, the prin-
11 cipal area of concern.

12 This other factor I have mentioned -- that is,
13 whether or not the ADR would be a means whereby a number
14 of securities as to which perhaps information was not generally
15 available would be introduced into the American market --
16 was a matter of concern to the Commission insofar as any action
17 it would take was an action which should be taken in the con-
18 text of the general public interest and the protection of
19 investors.

20 Where there was an area of some doubt and perhaps
21 alternative procedures available to the Commission, I think
22 the Commission in being persuaded to adopt the procedure
23 which it did was affected strongly by the arguments which
24 were presented to the Commission at that formal conference
25 and at conferences before and after that, that the ADR device

1 was sought largely to provide more ready transferability in
2 trading and securities which already enjoyed a market in the
3 United States.

4 To that extent, it was in the interest of investors
5 who already were financially interested in such companies
6 and in the interest of other investors who might wish to acquire
7 such an interest.

8 I merely want to make that perfectly clear for
9 the record.

10 MR. BROWNELL: I understand that. My point is only
11 that you cannot tear the web and completely dissociate the
12 existing owners of securities from those who might become
13 owners, because otherwise the Commission would have seen
14 fit perhaps in promulgating Form S-12 to limit its useability
15 to stockholders of foreign companies in this country who already
16 owned their shares.

17 The Commission did not attempt or even suggest
18 putting that kind of a limitation on the use of S-12.

19 MR. LOOMIS: I wonder if I could add just a little.
20 Although I didn't have much participation in the discussions
21 in 1955, I have the impression that this was considered at
22 that time as primarily a problem arising under the Securities
23 Act, the question of obtaining the registration and avoiding
24 the distribution of unregistered securities, while at the
25 same time, as you say, providing a convenient mechanism for

1 trading.

2 But there are questions, particularly when you get
 3 into the area of introducing securities not previously traded
 4 here and securities from countries where there are certain
 5 special problems -- questions arising under the Securities
 6 and Exchange Act, both with regard to the conduct of orderly
 7 markets and the question of whether, even assuming that
 8 there is no registration problem under the Securities Act
 9 for the underlying securities, the disclosures are adequate
 10 to meet the responsibilities of brokers trading in the ADR's
 11 in the market here who have an obligation to make disclosure
 12 to investors, who might be lulled into the belief and expect-
 13 tation that this problem under the ADR and S-12 is resolved.

14 MR. BROWNELL: Of course I don't know what went on
 15 inside the Commission. But as far as those of us who par-
 16 ticipated in the 1955 hearings and the discussion afterward
 17 are concerned, you are correct that we were studying the
 18 problem primarily from the point of view of the 1933 Act --
 19 although I assume everyone always had in mind the question
 20 of the 1934 Act in trading.

21 But the record of the 1955 hearing shows that the
 22 entire discussion revolved around problems of the 1933 Act.

23 MR. COHEN: Let me answer that, and I don't want
 24 to engage in any great discussion about what happened in 1955.
 25 But you will recall that a certain bank had acted in reliance

1 upon a letter that had been issued some years earlier,
2 which letter was concerned solely with the problem of registra-
3 tion under the 1933 Act.

4 The conference followed closely upon a reconsidera-
5 tion of that particular problem. The persons in attendance
6 at the conference were directing themselves primarily to
7 that issue, and the conference finally was designed to place
8 the Commission in possession of information and arguments
9 that the banks and other people wished to bring to bear on
10 that particular point.

11 I merely indicate that I thought I had made it per-
12 fectly clear to everybody who had an interest in this matter
13 that the Commission's concern was somewhat wider in scope,
14 and that in adopting S-12 it had in mind these various con-
15 siderations which Mr. Loomis has now spelled out in some de-
16 tail.

17 I might add in that connection that some of the
18 problems that we may discuss under the S-12 in our opinion
19 relate also to the underlying securities. There are problems
20 of the character that Mr. Loomis has discussed. These are
21 not problems created especially by Form S-12 or the ADR arrange-
22 ment; but to the extent that the ADR arrangement encourages
23 greater American participation in securities of this character,
24 it sort of widens the ambit of the problem, if there be a
25 problem.

1 MR. BROWNELL: Mr. Cohen, I don't want at this
2 stage to attempt to talk too much because I know there are
3 other gentlemen who would very much like to be heard on this
4 matter. But let me say only by way of supplementing what
5 you have said that I remember very well that you and Com-
6 missioner Woodside who perhaps were more actively engaged in the
7 details of the 1955 operation than other members of the staff
8 with whom we were in contact made it very clear at the time
9 Form S-12 was adopted that you were breaking new ground, and
10 the subject was one that you were going to follow closely.

11 Consistent with that desire on your part, Morgan
12 Guaranty Trust Company of New York and my firm have made it a
13 practice, as I think you will recall, of coming down at periodic
14 intervals of a year or a year and a half or two years and
15 informally discussing with either Commissioner Woodside or
16 yourself and members of your staff the way in which the S-12
17 machinery was operating.

18 We gave you figures showing the amount of ADP's
19 that were outstanding in the various issues, and we had
20 full and frank discussion -- always mindful of the fact that
21 this was a piece of machinery which should be operated, at
22 least as far as we were concerned, strictly in accordance
23 with the policies that you wanted to lay down.

24 Nothing formal was ever given to us by you or
25 Commissioner Woodside or any of the others at that time,

1 but the opinion was expressed that the procedures as we out-
2 lined them to you were in accordance with your general in-
3 tent. We hope always in connection with any ADR matter to
4 keep you fully posted on some of the policy questions that
5 are here today. We appreciate calling for your consideration
6 and we very much want to talk them over with you and come
7 to a joint conclusion as to what the best thing to do is.

8 MR. LOOMIS: I wonder if I could just add a quick
9 note to what I said before. I noticed an advertisement of the
10 local office of Merrill Lynch, which appeared in the last
11 couple of days, to the general effect that any foreign securi-
12 ties issues anywhere in the free world they would probably be
13 prepared to handle; and then they referred to ADR's as a
14 means for many of these transactions -- generally making it
15 look rather simple.

16 I am not criticizing this advertisement, but it does
17 indicate a growing, perhaps, trading problem.

18 MR. COHEN: Mr. Brownell, I just want to say one
19 further thing. I didn't intend by what I said to be critical
20 of Morgan Guaranty or what Morgan Guaranty has done. I really
21 used what you have said as a springboard for developing the
22 problem here -- if there is a problem; or at least explaining
23 what the dimensions of the problem are or may be.

24 Maybe it is the turn of some of your colleagues.
25 As far as I am concerned, since Jim started this thing, maybe

1 he ought to take over. Mr. Austin. From this point on, would
2 the speaker identify himself for the record. I am not
3 attempting in any way to control this discussion or to suggest
4 what should be said.

5 I would like the four points -- if there be four
6 points -- discussed in that order only so we may have a co-
7 herent record. But apart from that, bring in anything you
8 think relevant at all.

9 MR. AUSTIN: My name is J. A. Austin, Vice President
10 of Irving Trust Company. I want for the most part to identify
11 myself with Mr. Brownell's remarks as to the area which we
12 envisage as having been covered by the ADR and Form S-12 as
13 developed by the Commission.

14 We have, I am satisfied, taken such means as were
15 available to us to satisfy ourselves in every instance where
16 an ADR was issued by Irving Trust Company that it related solely
17 to a trading situation or an underlying security where the
18 (4)(1) exemption was available.

19 We have not consciously, I think, or unconsciously,
20 utilized the ADR to introduce trading into this country.

21 I am a little bit mystified myself as to the point
22 at which perhaps we have to limit ourselves. I take it that
23 the (4)(1) exemption, if it is available, we will say, to
24 1000 transactions of a given security a month, is also available
25 to any one, ten, or one hundred of them. So it raises the

1 question in my mind at least as to whether (4)(1) is avail-
2 able not only for existing trading but for such trading as
3 might exist, present or absent an ADR.

4 I have a little difficulty in that area.

5 MR. COHEN: Do you want me to respond to that?

6 MR. AUSTIN: If you would, yes.

7 MR. COHEN: I perhaps didn't make it clear. There
8 were two problems, I think, that the Commission considered
9 in determining whether or not it should adopt form S-12.
10 The first problem was the problem under the Securities Act,
11 the registration problem. I think as Mr. Brownell has indi-
12 cated, and as you suggested, despite your mystery, if there
13 is an exemption, there is an exemption whether it is ADR
14 or whether it is anything else, whether it is ten shares or
15 a thousand shares.

16 So that just by way of example, if Japanese securi-
17 ties were to be brought into the United States -- forgetting
18 ADR's for a moment -- under circumstances which did not re-
19 quire registration, there is no registration problem which
20 would prevent that from happening.

21 I think, however -- and I want to clearly emphasize
22 this -- that anyone who is responsible for causing the trading --
23 I am talking now about professionals and banks, to the extent
24 that they assist in this result in securing trading in the
25 American market or widening the scope of it -- may have certain

1 duties which spring from other sections of the Securities
 2 Act as well as the Exchange Act with regard to disclosures
 3 to investors and for the provision of information and
 4 things of that sort.

5 I merely want at the outset to indicate that,
 6 in adopting Form S-12, the Commission took into account those
 7 problems. In resolving those problems in favor of the
 8 desire of the banks and the trading community for a revised
 9 form such as Form S-12, the Commission was persuaded -- *Chief*
 10 wisely or otherwise; that is open to question -- that it was *of opinion*
 11 understood that Form S-12 was to be used largely to deal
 12 with the problem of securities that are already traded in
 13 the American market, although it was recognized that the ADR
 14 arrangement might widen the area of trading and maybe intro-
 15 duce additional securities.

16 But it was not intended to bring to the American
 17 market in any major way additional securities as to which
 18 this basic problem of the man engaging in trading would have.

19 In other words, this was a problem of the Commission's
 20 responsibility as an agency of the Government concerned gener-
 21 ally with the injunctions and the statutes to assure that its
 22 actions are in conformity not only with the statutory require-
 23 ments, but the standards of the Act as well.

24 Those standards are reflected in a web of provisions
 25 which were designed to secure the results that I have mentioned.

1 That is what I meant.

2 MR. AUSTIN: I certainly agree with you, Mr. Cohen.
3 I might say, so far as we are concerned, that self-interest
4 would have dictated that we would not want to make ADR's
5 available in cases where there was not established trading.

6 Whether or not the fact of the introduction of
7 an ADR where trading was established resulted in more of it wa
8 something that we all foresaw it might. It has in many in-
9 stances resulted in less of it for reasons not having to do
10 with ADR's.

11 MR. COHEN: I want to emphasize what I said a few
12 minutes ago. It was recognized that the ADR would in some way
13 stimulate investor interest in securities. Perhaps the
14 answer is that we didn't envisage -- I may be wrong about
15 the facts -- quite the stimulation that it has received.

16 I think what we are doing here today is learning
17 more about the problem to permit us and the Commission to
18 assess the problem, if there is one, to determine whether
19 or not this ADR or S-12 arrangement needs reconsideration and
20 review, whether other procedures are necessary, or whether
21 everything is going along in such a happy fashion that the
22 Commission and the industry can feel proud that the proper
23 form is the S-12. That is it.

24 MR. AUSTIN: I think we understand that. Insofar as
25 disclosure problems are concerned -- and I have in mind now

1 particularly the Japanese issues which are the subject
2 initially, I take it, of these hearings; at least they
3 bring the problems to a head -- I believe it is a fact so far
4 as we are concerned at least that we have not yet been satis-
5 fied that we have satisfied the Commission or members of
6 the staff as to whether disclosure on the registration state-
7 ment relating to Japanese securities which we have filed
8 have been fully met.

9 That was a subject that I think as a matter of
10 practical consideration we let ride until the S-1 became effec-
11 tive. I think we all felt that that, being a full registra-
12 tion under the Act, could be the bellwether here.

13 That of course, as we recognize, stands on its own
14 feet insofar as the two million shares of Japanese stock
15 are concerned, when one registers with an underwriter.

16 I think, however, there was still open the dis-
17 closure problems relating to all of the ones on S-12, whether
18 effective, or effective subject to a delaying amendment.
19 That is a matter which is, I take it, one of the reasons
20 why we are here.

21 MR. COHEN: Yes, indeed. Have you concluded whatever
22 you thought you ought to say with regard to the first prob-
23 lem?

24 MR. AUSTIN: This aspect of it, yes; I have.

25 MR. COHEN: I have been led to understand -- I am

not sure that I have all the facts -- particularly with respect to the ADR's for Japanese securities the demand for ADR's in this area was not a demand voiced by the trading community, but that this was something the banks undertook on their own initiative.

If that is wrong, I would like to get the facts to the extent that you or any of your colleagues can deal with the situation and perhaps explain how the Japanese ADR's came about, because the filings were pretty close in point of time.

MR. AUSTIN: Let me answer that by saying, Mr. Cohen, I am not aware of a specific demand from the trading community - to use your language -- for an ADR in the case of -- and I limit myself to our own action -- those registration statements which we filed for five different Japanese securities.

We have filed -- and I want the record to show this -- for Fuji Island Steel, Kitashi, Limited, Mitsubishi Chemical, Nippon Electric and Mitsui Shipbuilding.

During fiscal 1960 there were outstanding in foreign holdings, in the case of Fuji in the amount of 660 million shares, 320,000 shares held abroad, most of which we are advised was in the United States -- the number of stockholders being 539.

In the case of Kitashi, out of a total number of shares outstanding of 600 million, there were during fiscal

1960 4,494,000 shares, with 1620 stockholders among foreign holders, most of them in the United States.

Mitsui Shipbuilding, out of 90 million shares outstanding, 293,000 shares among the foreign holdings, with 70 stockholders.

Mitsubishi Chemical, out of 119 million shares, 495,000 shares here, with 139 stockholders.

And Nippon Electric, out of 160 million shares, 35,200,000 shares here, with 92 stockholders.

On the basis of that, we filed the ADR. We satisfied ourselves as to that type of distribution, that availability for trading in this country before proceeding. I will not go so far as to say that, in preparing to discuss this and preparing to file S-12 registration statements covering these things, that we consciously answered a conscious demand by the trading community. But we assumed there was such a demand.

MR. COHEN: May I ask this in regard to the Japanese situation. In respect to other ADR arrangements which Form S-12 registration is filed on behalf of by Irving Trust Company, did those situations come about as a result of a demand by the trading community for an ADR, or again has that been something that the officials of Irving Trust Company have undertaken to do for reasons similar to those you have just expressed?

1 MR. AUSTIN: I would say in most of the cases of the
2 European ones, there has been a demand expressed to us by the
3 trading community.

4 MR. COHEN: To this extent, the Japanese situation
5 is different than the other ADR's.

6 MR. AUSTIN: I think so; I think so.

7 MR. COHEN: Have you anything more you want to say
8 at this point?

9 MR. AUSTIN: Not at the moment, but I will on other
10 aspects.

11 MR. COHEN: May we pass to the next bank. *Wolfe*

12 MR. CARR: My name is William D. Carr. I am Vice
13 President of the Chemical Bank and Trust Company. We recognize
14 the policy of the Commission that ADR's shall not be used
15 to introduce de novo trading in foreign securities in the
16 American market.

17 We satisfy ourselves in each instance that there is
18 trading before we file the S-12's.

19 Actually, bearing out what Mr. Austin said, the
20 almost invariable pattern is that we get calls from dealers
21 telling us that there is trading in a certain security, and
22 they think trading would be facilitated by the ADR procedure.

23 I also agree with Mr. Austin that the Japanese situa-
24 tion is a little different. I believe there the pressure
25 originally came from Japan rather than from the trading

1 community. I believe a visit was made a year or so ago
2 to Japan by one of the banks, and that did stimulate a
3 tremendous interest -- as a matter of fact, a petition among
4 the various Japanese companies -- to acquire face through the
5 ADR procedure.

6 I think to that extent the Japanese situation is
7 different. I will reiterate that in all other cases the
8 initiative comes from the trading community.

9 For the record, I would like to say so far as our
10 Japanese filings go, we have filed for Tokyo Shikora Electric
11 Company, of which there were 1216 holders as of January 25,
12 1961, which is the latest figure I have here. Those shares
13 are worth at the then market price around \$3,690,000.
14 Yawata Iron and Steel Company, 1160 holders; market price,
15 \$1,290,000. Mitsubishi Heavy Industries Reorganized,
16 355 holders; market price, \$383,000. Mitsubishi Shoji Kaisha,
17 118 holders; \$288,000 market price; Maruzen Oil, 77 holders;
18 market price, \$82,000.

19 I believe that is all to that particular point.

20 MR. COHEN: Do we have any other banks here?

21 MR. ROBERTSON: I am James E. Robertson, First
22 National City Bank of New York. Let me be quite frank in
23 saying that we are comparative newcomers to the ADR field.

24 We are an international bank. We are the oldest
25 and largest American bank in Japan. We felt that, with the

tremendous interest in Japanese ADR's, to preserve our competitive position we should go into the ADR arrangement.

We did, however, verify before filing on the five issues which we have filed with the Commission that there was a substantial foreign interest in the shares of those five ADR candidates.

We are not duplicated on any of our issues. We will not duplicate any ADR issues.

MR. COHEN: Do you have any figures comparable to those of Mr. Austin?

MR. ROBERTSON: On Yawata Iron and Steel, 947,000 shares. On Kansai Electric Power, 403,000. On Mitsui and Company, 627,000. On Tokyo Fire and Marine, 442,000. And on Nippon Tool, 2,570,000.

MR. LOONIS: Do you have any figures as to the number quoted?

MR. ROBERTSON: No, I don't at this time. I can provide those later if you wish.

MR. LOONIS: We would like to have those.

MR. COHEN: Just so we have it in one place in the record: Mr. Brownell, do you have comparable figures?

MR. BROWNELL: Mr. Moxley may have them. If he hasn't got them with him --

MR. MOXLEY: No. You have the figures because, of our five accounts, four of them were duplicated. You

1 already have the figures on four of them attached to the
2 statement on Ansonia. Of course that is our own account.
3 There is no question of duplication because there we have
4 the public offering of the two million shares.

5 I would like to say this, Mr. Cohen, on Japanese
6 ADR's. This was not something new with Morgan Guaranty
7 Trust Company of New York because as far back as the latter
8 part of 1955 and the early part of 1956 we visualized where
9 there was going to be, at least in our opinion, a terrific
10 economic expansion in Japan.

11 It seemed to us that the building of economic ties
12 between Japan and the United States had become closer --
13 which I think since has become borne out. In 1956 we took
14 up with our good correspondent bank over there the question
15 of the mechanism of creating ADR's for Japanese securities.

16 There was a terrific language problem in getting
17 the correspondence back and forth that left a lot to be de-
18 sired. The Minister of Finance in 1956 was of the opinion
19 that, while he fully appreciated that Japan needed foreign
20 capital, and while ADR's would not give it to them because
21 they could get that by their debt issues, they thought it
22 was a little bit premature.

23 So while we saw continued American interest in
24 Japanese securities, we did re-approach the problem just a
25 year ago. I am sorry to say in a way there was publicity

1 given to this question in Japan that was out of all propor-
2 tion to the purpose for which it was intended. But these
3 things got out of control over there, and I am sure no harm
4 was done.

5 I just wanted to give you that background so you
6 would know that this was not something we have not been
7 thinking about and have not been studying and just picking
8 out of the air quite recently.

9 MR. COHEN: I would like to go back to Mr. Austin.
10 I think these figures represent foreign holdings of Japanese
11 securities?

12 MR. AUSTIN: That's correct.

13 MR. CARR: American holdings.

14 MR. COHEN: I think he said foreign. That is what
15 I am trying to clarify. You said they were largely American?

16 MR. AUSTIN: Largely American.

17 MR. COHEN: How did you determine that, Mr. Austin?

18 MR. AUSTIN: By the advice of various houses on the
19 street who were active traders in these shares.

20 MR. COHEN: You actually did talk to the various
21 houses?

22 MR. AUSTIN: Yes, we did. That is our only source
23 of that information.

24 MR. COHEN: Mr. Carr, did you want to add some-
25 thing?

1 MR. CARR: Yes. We were told by the Japanese secur-
2 ities houses that at least 95 percent of those figures I
3 gave represent American holders. In essence they are Ameri-
4 can holders.

5 MR. AUSTIN: We were told the same thing.

6 MR. ROBERTSON: That was also the source of our
7 information. Those are foreign holdings, not broken down.

8 MR. COHEN: You said you tested the market. Is
9 that what you meant by testing, or did you have something else
10 in mind?

11 MR. ROBERTSON: We talked with the securities houses,
12 primarily the Japanese securities houses.

13 MR. COHEN: For what purpose?

14 MR. ROBERTSON: To determine how many of those shares
15 and what proportion were held in this country.

16 MR. COHEN: Did your testing encompass any other
17 inquiry?

18 MR. ROBERTSON: Along what lines?

19 MR. COHEN: I am not sure; I am asking you whether
20 there were any other lines.

21 MR. ROBERTSON: No. I think that is the only test
22 we made.

23 MR. AUSTIN: You understand, Mr. Cohen, that these X
24 Japanese shares are not available physically in this coun-
25 try. They remain in Japan.

1 MR. COHEN: Are there any other banks represented
2 here?

3 MR. TRAVERS: I am Edward Travers, Vice President
4 of the Manufacturers Trust Company. I appear as an observer.
5 We are not in the ADR situation as yet, but we may be.

6 MR. COHEN: If you have any views, Mr. Travers,
7 that you would like to express, we would like to have them
8 now on this particular point.

9 MR. TRAVERS: I don't think I am qualified to
10 express any views. I would rather sit and listen, I think.

11 MR. COHEN: All right, sir. Mr. Brownell, you
12 suggested earlier you would be glad to tell us what the pro-
13 cedures of the bank are with respect to the problem of determin-
14 ing or assuring yourself that there is no registration problem
15 when you engage in ADR arrangements.

16 I don't know whether you prefer to discuss that
17 now or prefer to provide us with a memorandum in which you
18 would indicate what the procedures of the Morgan Guaranty
19 Bank are, which we would then make available to the Commission.

20 - If that is the procedure you would prefer, I will
21 accept that. I make this statement to all you other gentlemen,
22 that if you want to tell us here as a matter of record how
23 you do this and what steps you take, we would be glad to take
24 it.

25 But if, on the other hand, you prefer to submit that

1 by way of separate memoranda, that is agreeable to me.

2 MR. BROWNELL: If I may, I will do both -- but make
3 my oral statement very brief in view of your giving us the
4 privilege to supplement it in any memorandum more specifically.

5 MR. COHEN: I recognize there is a certain difference
6 of view around this table. It is not necessary for our pur-
7 poses today, I don't think --

8 MR. BROWNELL: In order to cover the point you have
9 mentioned, Morgan Guaranty never goes forward with an ADR
10 issue until they have set up machinery, either through one
11 of their branches in Europe -- those branches are located in
12 London, Paris and Brussels -- or through correspondent banks
13 whereby the branches or the correspondent banks keep in
14 close touch with the issuer so that they will become imme-
15 diately familiar with any new offering of securities.

16 Morgan Guaranty is also in close touch in all cases
17 with the issuer. They do not go forward with an issue until
18 they have established contact with the issuer. They receive
19 notices, of course, in their capacity as record holders, of
20 the underlying shares -- which in a great many cases would
21 put them on notice of any new issues of securities.

22 They make careful inquiry to assure themselves
23 that there is no control situation existing. In the case of
24 these large companies, as I am sure you know, it is not very
25 difficult to determine whether or not there is any

controlling block -- as this Commission itself uses the word "controlling."

Where new issues originally offered in this country that would have to be registered are involved, the bank does not accept deposits of the new stock until the statutory period has elapsed; and also even goes so far as to make inquiries to be sure that there are not unsold blocks in the hands of dealers or other blocks which over here would come under the general heading of "hot stock."

We have also considered getting either the depositing stockholder himself or the broker or dealer acting on his behalf to file a certificate which will certify in language following the language of the Act that the stock being deposited is not stock that would have to be registered or sold publicly here.

We are giving particular consideration to requiring such forms of certificate in connection with Japanese issues, and all others, as Mr. Moxley points out. We will be more than glad, if the Commission is interested, to submit the form that we propose using -- copies of which I have here with me, for such certification as a further preventative of the issuance of ADR's against "hot stock."

The problem is somewhat facilitated in the case of many of the foreign countries by the fact that new offerings of securities are represented by allotment letters and other

pieces of paper which can be readily identified, and that the certificates for the new stock itself don't become generally available until after the distribution is completed, when the stock is no longer "hot."

MR. COHEN: We would like to have copies of the documents.

MR. BROWNELL: I will be glad to give them to you at the close of the hearing.

MR. COHEN: Thank you.

MR. AUSTIN: I would like to say, Mr. Cohen, with respect to that, we went further at the time we filed our original ADR's and had as an exhibit to the registration statement an enlargement form which paraphrased the language of the Act, which constituted a certification by the broker or dealer depositing the underlying shares.

We made sure by our London agent that the stock was not within the category that would be required to be registered under the 1933 Act. Some years subsequently we discovered that we were alone in that requirement; that it was considered onerous by our English friend; and we amended it out.

I regret that we amended it out, and we are going to reinstate it, perhaps in somewhat simpler language. In fact, I think we have submitted to the Commission the kind of language, somewhat boiled down, which we will henceforth

1 require as a further assurance to us that we have made the
2 various attempts at assurances that Mr. Brownell has describe
3 as a further assurance in written form on this point.

4 MR. COHEN: Did you say that the boiled-down new
5 version has been filed with the Commission?

6 MR. AUSTIN: Not filed; it was submitted, together
7 at the time we submitted suggested language for a further
8 legend on the Japanese agent.

9 MR. COHEN: Mr. Carr, do you want to add something
10 to this discussion?

11 MR. CARR: I would say generally that our London
12 office and our London depository and our New York and other
13 depository banks in the country are alert to the problem and
14 they will not accept stock which they know to be "hot stock."

15 As far as the rights offerings go which are fairly
16 numerous in some of the foreign countries, it isn't too much
17 of a problem. It is a slightly more difficult problem to
18 tell whether a particular lot of stock comes from control or
19 not; but they are alert to the problem and I think they have
20 solved it, so far as I know, in every case

21 There was some discussion a while ago among the
22 four banks as to a form of broker certification. I want to
23 reiterate what Mr. Austin said, that it has been submitted
24 informally to you and we will be very glad to cooperate with
25 you in seeing that these are filed before ADR's are issued.

1 MR. AUSTIN: I would like to add simply, Mr. Cohen,
2 that the original allotment form which we have filed still
3 obtains as far as we are concerned.

4 MR. ROBERTSON: We will follow the same procedure,
5 Mr. Cohen, and get a representation from the broker before
6 he takes delivery of the ADR -- the representation to be
7 in the form previously submitted to the Commission.

8 MR. CARR: There is some question of whether the
9 representation should be made by the American dealer and sub-
10 mitted to the American bank at the time ADR's are issued; or
11 whether it should be as Irving originally had it, by the forei
12 depositing broker depositing the shares abroad.

13 I don't believe we have yet resolved that problem
14 among ourselves.

15 MR. COHEN: If you are asking me for a tentative
16 expression of view, I would think the American broker should
17 do that.

18 MR. CARR: We have come to that tentative conclusion
19 at least three of us have.

20 MR. COHEN: Coming back to Mr. Brownell with referenc
21 to the allotment letters: Do I understand properly that you
22 had reference to those in regard to the possible question
23 whether any of the shares come from a person who be "an
24 underwriter" as distinguished from a control person?

25 MR. BROWNELL: I had reference more to the period of

1 time that had elapsed between the date of the original offer-
2 ing and the date of the tender of the securities for deposit
3 against the issuance of an ADR, because the certificates
4 of new stock under the practice of foreign countries don't
5 get out into circulation into the market for a period of
6 time.

7 In the meantime the allotment letters represent the
8 rights. It was the period of time I had in mind.

9 MR. COHEN: Then perhaps you ought to pursue this
10 a little further. You have talked about assurance that the
11 shares don't come from control sources or persons having a
12 control relationship, which I think is more nearly the statu-
13 tory test.

14 What steps do you take to assure yourselves that
15 the shares or securities are not coming from a person who may
16 be a statutory underwriter?

17 MR. BROWNELL: We take steps to become informed when
18 there is any public offering of shares. We are alerted when
19 we have word of a public offering. You broaden the question
20 to include someone who might be in a position of underwriter
21 on a small scale where he purchased securities directly
22 from the issuer with a view to distribution; but there was
23 not a generally recognized public offering of which our
24 representative would have notice.

25 MR. COHEN: Yes, sir.

1 MR. BROWNELL: There might be a possibility of that
2 kind. That is one of the reasons why we are proposing to
3 adopt the form of certificate. I doubt very much if the
4 number of shares involved in such a situation would be very
5 large, but it is to give further protection against that kind
6 of thing that the bank is going to make use of the form of
7 certificate to which I have referred.

8
9 MR. COHEN: Mr. Austin, is your enlargement form
10 designed to cover that situation as well?

11 MR. AUSTIN: Yes, definitely. But there is a
12 further assurance as far as we are concerned, Mr. Cohen,
13 and that is this. We have a London agent -- one of our
14 correspondent banks, the National Provincial Bank. There is
15 on file with the Commission as part of each registration
16 statement the agreement between ourselves and our London agent.

17 They in that agreement undertake to see to it
18 that the category you mentioned is not made available for
19 issuance.

20 MR. COHEN: You understand, Mr. Austin, that I am
21 familiar with that. We have discussed it many times. I
22 want to get it in this record.

23 MR. AUSTIN: I understand.

24 MR. COHEN: Do any of the banks want to speak further
25 to this problem before we pass on to the trading community?

Mr. Froy, I take it you are a representative of the

trading community. Will you identify yourself and speak to this problem or any aspect of it that you think would be relevant to our discussion and helpful to the Commission, to the banks, and -- more importantly -- to the investing public.

MR. FROY: I am H. L. Froy, Chairman of the Foreign Securities Committee of the NASD, and a partner in Abraham & Co., members of the New York Stock Exchange.

Before I answer your question, may I say that we are most grateful that S-12's are in existence. We are also very pleased that we have the facilities of ADR's.

Before I answer any further questions, may I for the benefit of those who are not members of the NASD take a few seconds of your time to explain the purpose of our Association. The banks are not members of the NASD. This, I am sure, will assist you to understand why we must first and foremost fight for the protection of the public, the final end of the chain of all our projections.

The purpose of the NASD is to promote, through cooperative effort, the investment, banking and securities business; to standardize the principles and practice; to promote the high standards of commercial honor; and to encourage and promote amongst members observance of Federal and State security laws.

Secondly, to provide a medium through which its

1 membership may be enabled to confer, consort, and cooperate
2 with Government and other agencies in the solution of problems
3 affecting investors, the public, and the investment securities
4 business.

5 That is as far as I will go about the NASD.

6 I believe I will not have to state -- as was re-
7 cently done by a member of the SEC in answering questions of
8 Lord Jenkins in London -- that the remarks that are made here
9 today are mine and not necessarily those of the Commission;
10 nor that they do necessarily reflect the views of the Associa-
11 tion nor my colleagues on the committee.

12 We feel that the discussion which has taken place
13 so far is probably in an area which is very surprising. We
14 feel that the issuance of ADR's by the banks is a service of
15 which we avail ourselves and pay for it very dearly. The
16 banks are doing a very useful service, but they are under
17 the impression that the broker-dealer community would be
18 completely lost if ADR's would not be issued by banks.

19 I believe there are other facilities. I believe
20 that the broker-dealers could get together and create their
21 own issuing machinery, and would run this on a non-profit
22 earning basis. There is absolutely no reason why we shouldn't
23 arrive at that point; and the 3-12's which are available could
24 be filed by such an organization and the public would have
25 the ultimate benefit of such an arrangement.

1 We have been told that the banks feel that competi-
2 tion is good for business. The first ADR was issued around
3 1925, and competition has been going on ever since. I do
4 not believe that the ADR rates through competition have ever
5 been reduced.

6 We on behalf of the public are paying for this fa-
7 cility.

8 You have discussed in particular Japanese ADR's
9 today. I maintain that the brokerage community did not ask
10 originally to have the facilities of ADR's until such time
11 as we would file that we could maintain an orderly market and
12 would in no way deceive the public. By deceiving the public,
13 I mean we should have facilities to explain in simple language
14 the risks they are running in acquiring such foreign securi-
15 ties.

16 We have so far succeeded in doing this in most
17 other foreign securities prior to the issuance of ADR's
18 because -- as Mr. Cohen puts it -- there are two different
19 animals who are dealing in foreign securities; those who
20 originally buy foreign securities before ADR's are issued,
21 which is the result of our discussions explaining certain
22 reasons why they would like to be investing in foreign
23 securities; and those investors who buy ADR's because they
24 are under the impression that this instrument has been created
25 with the permission of the SEC and with the help of the NASD

1 and with the great assistance of the banks.

2 This is probably creating a very false impression
3 to the investor. It does make our position extremely diffi-
4 cult because the type of investor who buys an ADR is generally
5 the small investor and not the very large investor.

6 The large investor does not feel that he has to
7 avail himself of the facilities of the ADR's. He feels he
8 can save this money and have even the benefit of other facili-
9 ties which he could not have under the ADR arrangements.

10 I don't think I want to say any more about this
11 situation now because the question of duplication, I am sure,
12 is going to come up later.

13 I would only like to point out that we are actually
14 the beneficiaries of those ADR's. But I think the banks are
15 under a great misapprehension if they think they can force
16 our hand the way they have been doing it in the case of
17 Japanese securities.

18 MR. COHEN: Did you want to respond to that state-
19 ment, Mr. Brownell?

20 MR. BROWNELL: I don't want to respond to most of
21 it because I think most of it is completely outside of the
22 four questions which you said we were here to discuss. (1/18/64)
23

24 But Mr. Froy did indicate that he thought the use
25 of ADR's for Japanese securities involved an element of
26 deceit because it was not possible to expose certain

1 characteristics of Japanese stocks in connection with the
2 ADR's.

3 I point out first that our proposal involves a
4 great deal more disclosure than is required under any list-
5 ing proposal or practice with respect to the sale of Japanese
6 stocks that are not represented by ADR's; and I wanted to ask
7 Mr. Froy if the comments that he made under that rather
8 difficult word "deceit" which apply to ADR's would not equally
9 apply to the sales in this country of shares in Japanese
10 companies.

11 MR. FROY: I did try to make this question very
12 clear. Maybe you haven't heard. I explained it. If we try
13 to sell or deal in underlying securities, that means originally
14 Japanese securities, we are dealing with a different type
15 of investor who invariably gets a full explanation from us
16 verbally when he wants to take an interest in foreign securi-
17 ties.

18 MR. BROWNELL: Suppose some other firm does not
19 confine itself to dealing with the large investor. Would
20 the answer to my question with respect to them not be the
21 same with respect to the sale of Japanese stock and with
22 respect to an ADR, except perhaps in connection with the ADR
23 there might be a greater disclosure than that to which you
24 referred?

25 MR. FROY: Not on the ADR's which I have in front

1 of me. But in principle that is what it should be. But in
2 our opinion it is insufficient. Besides, the average in-
3 vestor does not see the ADR probably ever.

4 MR. BROWNELL: But you do agree that the question
5 you raised under this -- I think inappropriate -- word
6 "deceit" would apply equally --

7 MR. FROY: You say we deceive?

8 MR. BROWNELL: -- to ADR's?

9 MR. FROY: No, because I have told you that in the
10 case of the man who wants to invest in a foreign security,
11 we would go to any length of time to explain to him the risks
12 and the dangers and the restrictions. That is what we have
13 in the ADR -- where the idea has been created that this
14 is the New York market, which is an easy trading market, and
15 you cannot go to the same --

16 MR. BROWNELL: Why couldn't you make exactly the same
17 disclosure here with respect to the sale of an ADR that you
18 would with respect to the sale of a stock represented by that
19 ADR?

20 MR. FROY: Because there is a very much larger demand
21 generally for an ADR than there is for the normal share before
22 an ADR is issued.

23 MR. COHEN: May I say two things about this dis-
24 cussion. First, Mr. Froy attributed to me some statement about
25 two different kinds of animals. I am sure all of you understand

1 I was not referring to any investor -- whether he is sophis-
2 ticated or unsophisticated -- as an animal. The second thing
3 I want to say is that, while I did list the four points that
4 I thought should be discussed here -- and I should have made
5 this clear at the outset -- I didn't intend to limit our
6 discussion to the four points.

7 I think everything that is relevant to the ADR
8 situation should to the extent possible be developed in this
9 record. For your information, I have in mind that this
10 record will be provided to each of the Commissioners so
11 that each one of them can consider the problems to the extent
12 that we identify and discuss problems here today.

13 I think our reference to two different situations
14 related to a discussion I had with Mr. Froy in which I had in
15 mind that there may be a distinction so far as investor inter-
16 est is concerned and public interest is concerned between the
17 professional arbitrageur, who theoretically at least is sophis-
18 ticated in all of the nuances of the problems; and the ordinary
19 investor, who may be considered part of a mass market or what
20 may be hoped to be a mass market, and the sort of thing Phil
21 Loomis referred to when he adverted to the advertisement of
22 Merrill Lynch.

23 I don't mean by this, nor did he mean by this,
24 to suggest that Merrill Lynch is improperly advertising. But
25 it is an indication of the desire -- and there is no reason why

1 it shouldn't be carried on this way -- to attract a wider
2 interest and therefore more of a mass market in an area which
3 as I understand Mr. Froy, has traditionally been confined to
4 a smaller and a more sophisticated market.

5 I think that is the point that we were discussing.
6 I didn't mean to quarrel with anything you said, Mr. Brownell
7 I merely am trying to explain the allusion.

8 Are there any other representatives here of the
9 trading community who wish to be heard on this point?

10 MR. FROY: I will agree to state the members
11 of the Foreign Securities Committee with reference to their
12 feeling about Japanese ADR's from our minutes, which are
13 confidential, by the way, and are not published otherwise, or
14 are not supposed to be published.

15 MR. EHEN: My name is Howard Ehen. I am the Secre-
16 tary of the Foreign Securities Committee of the National
17 Association of Securities Dealers.

18 MR. COHEN: Before you proceed, the reference you
19 made to confidentiality: This is not a public hearing in one
20 sense, but there are no restrictions on what we say here today.
21 Of course the Commission will have it, and what we say here
22 today may become a matter of public record in another forum.

23 MR. FROY: I have permission from our Executive
24 Director to have these minutes read, if you would like.

25 MR. COHEN: Thank you.

1 MR. EMEN: There were discussions with regard to
2 the issuance of ADR's, and particularly the Japanese regula-
3 tions. The entire Committee voted as one in favor of this
4 resolution: Write a letter to the SEC explaining the feeling
5 of the Committee that it is necessary for changes to be made
6 in the existing Japanese regulations to protect the public.

7 The regulations at present are not acceptable to
8 broker-dealers who have to make primary markets in these
9 securities.

10 At another meeting, June 2, members agreed unani-
11 mously to send a telegram to the SEC suggesting the Sony
12 registration be approved as a pilot issue; the approval of the
13 issue of all of the ADR's to be held up until the foreign
14 exchange regulations could be eased, until the Committee
15 could evaluate the Sony operation.

16 I may be going ahead too much. There are two
17 other meetings with regard to duplication.

18 MR. FIDY: We will wait until we come to that.

19 MR. COHEN: Thank you. Is there any representative
20 here of a Japanese securities house? Is there anybody here
21 authorized to speak on behalf of the Japanese securities
22 houses or a Japanese issuer or any representative of the
23 Japanese Government here, or any part of that Government?

24 MR. JAMES DOYLE: I think perhaps the record should
25 show that the absence of these interests which you have just

1 mentioned is not due to their lack of interest in this subject;
2 but perhaps because it wasn't understood that their interests
3 should be expressed here at this time. I don't know that
4 any invitations were extended to them.

5 I think the same might be said for the section of
6 the trading community that is represented by that ad. They
7 obviously have their points of difference with the presen-
8 tation which has been made.

9 MR. COHEN: May I take advantage of the fact that
10 you did volunteer your statement. If you are familiar with
11 the points of difference and care to express them, we would
12 appreciate having you do so.

13 MR. JOSEPH DOYLE: I am not, Mr. Cohen. I am a
14 representative of the First National City Bank here; but I
15 think it is proper that the record not leave an indication
16 that the Japanese securities houses would not like to express
17 a presentation on whatever their point of view is. I don't
18 know what it is.

19 But they are simply not here, and I don't know that
20 they were asked to be here. Merrill Lynch, of course, couldn't
21 have known that its name would be discussed.

22 MR. LOOMIS: Since Merrill Lynch's name was dis-
23 cussed, I think it only reasonable to say that that advertisement
24 contains no mention of Japanese securities. I presume it was
25 not addressed to that particular problem.

1 MR. FROY: May I just say that one of the partners
2 of Merrill Lunch and Company is a member of our Committee.
3 He was of the same opinion as the one stated by me and
4 covered by the minutes read by Mr. Egan.

5 MR. COHEN: Mr. Froy, may we take advantage of the
6 fact that you are probably most familiar with the attitude
7 of the trading community. If there are minority views which
8 you think might be helpful to the Commission in this area,
9 despite your disagreement with them, if you do disagree
10 with them, we would appreciate it if you would indicate what
11 the minority views are.

12 MR. FROY: Mr. Cohen, I believe Mr. Moxley is more
13 qualified to answer this question, as he has been in touch
14 with the trading community actively over the last two weeks
15 to cover their views and have the necessary information at
16 his disposal.

17 He even contacted firms who are members of our
18 Committee. I think his information is more accurate than
19 mine.

20 MR. COHEN: Before I ask Mr. Moxley whether he
21 wishes to address himself to this point, I want to deal with
22 another point that has been made. I issued no written invita-
23 tions to anyone. I did indicate -- and I think this received
24 some wide circulation -- that I would appreciate those of you
25 who are interested in this problem making known the fact that

1 we were going to have this conference, and that we would like
2 to have in attendance at the conference anyone who might
3 bring to the Commission information or arguments which were
4 relevant or might be helpful to a consideration of the
5 problem and resolution of the problem.

6 We did not intend to exclude anyone. I think that
7 I indicated to Mr. Froy that anyone who wished to come and
8 express a view was welcome. If this did not receive as wide
9 circulation as I thought it had, then I am sorry. But we
10 didn't intend to exclude anyone and had no such intention.

11 MR. LOOMIS: It might be mentioned in that connec-
12 tion that there was an article in The New York Times last
13 Sunday which reported that a meeting with reference to
14 Japanese ADR's was going to be held -- although the article
15 didn't extend a public invitation to attend.

16 MR. COHEN: Mr. Stevenson, did you want to say
17 something? Would you identify yourself?

18 MR. STEVENSON: I am a partner in Sullivan and
19 Cronwell. We represented the managing underwriters in the
20 Sony financing. One of the managing underwriters was,
21 of course, a Japanese securities firm.

22 One point that I would like to make from the stand-
23 point of managing underwriters of Japanese securities is that
24 ADR's are of course very useful in connection with a public
25 offering of Japanese securities. I think there is practically

1 no opposition on that point, that when there is a fully
2 registered public offering it is a great convenience to the
3 American purchasers who are receiving the new securities
4 in having ADR's rather than in having the underlying shares
5 offered.

6 I think it also may be said that the prospective
7 investor has a better idea of what he is getting if there
8 have been ADR's traded in the United States previously so
9 that I think there is a certain plus that has to be weighed
10 against some of these considerations that have been mentioned
11 the other way in having existing an ADR market before a new
12 offering of a foreign security is made.

13 I am not authorized as far as this particular hearing
14 is concerned to speak on behalf of any of the Japanese firms,
15 but it is certainly my impression that -- subject to any cor-
16 rections that may later be made -- the ones that I talked
17 to are definitely in favor of having ADR's as well as under-
18 lying securities. But I make that as an observation rather
19 than as a statement on their behalf.

20 MR. CONEN: I would only add one further thing to
21 this point that has been raised about attendance at this
22 meeting. I now wish to extend to any Japanese firm or any
23 other firm the opportunity to submit to us any memoranda
24 that they think relevant or helpful in connection with any
25 of the matters we have discussed today or any other matter

1 relating to the entire Japanese ADR situation.

2 MR. BROWNELL: Mr. Cohen, may I say a word?

3 MR. COHEN: Surely.

4 MR. BROWNELL: With respect to one of the things
5 Mr. Froy has just said -- and of course this Commission, and
6 I am sure everyone else here, has the greatest respect for
7 an expression of opinion by any committee of the National
8 Association of Securities Dealers -- I would like to
9 take the time to go further into that resolution so we may
10 clearly understand the reasons for it.

11 As I understood it from what Mr. Froy said of the
12 effect of the resolution itself, the Foreign Securities Com-
13 mittee of the NABD believes that the existing Japanese foreign
14 exchange restrictions are not in all respects satisfactory
15 from the point of view of American holders of Japanese stocks.

16 That was, as I understood it, the only reason that
17 was given that prompted the request to the Commission that
18 these American depositary receipts for Japanese securities
19 not be approved or -- to state it more accurately -- that the
20 registration statements regarding these ADR's not be allowed
21 to become effective.

22 I would like to ask Mr. Froy if that is the reason.
23 Also, if that be the reason, I would like to ask whether
24 exactly the same argument would not apply to the purchase by
25 American residents and citizens of shares of stock in

1 Japanese companies.

2 MR. COHEN: You have anticipated my next question.
3 I would appreciate an answer to that, too, Mr. Froy.

4 MR. FROY: I do not think that I have a right to
5 a answer this question because the authorization for those
6 non-issued ADR's was held up by the SEC and only on advice
7 of the NASD. But the final decision is with the SEC.

8 MR. COHEN: Maybe I misunderstood the question.
9 I thought Mr. Brownell was asking another question other than
10 that.

11 MR. BROWNELL: That's right.

12 MR. COHEN: Perhaps you will restate it yourself.

13 MR. BROWNELL: Mr. Cohen is quite right. You have
14 not answered my question. I stated that it appeared to me
15 from what you said that the reason for one delay, and the
16 objection to the issuance of ADR's on behalf of your Committee,
17 was the existence of certain Japanese foreign exchange regula-
18 tions.

19 Since that is the fact, I ask you whether exactly
20 the same objections and reasons wouldn't apply to the sale
21 of Japanese shares that were not represented by ADR's.

22 MR. FROY: Mr. Brownell, I would very much like
23 to answer your question, but that comes into an area which
24 we will probably cover later -- and that is the question of
25 duplication of ADR's where it is extremely important that this

1 question be answered in that connection.

2 Anyhow, the restrictions at the moment on foreign
3 investments in Japan are so complicated that many of the
4 professionals do not even fully understand them. If you
5 read the disclosure on top of the Sony ADR, which was approved
6 by the SEC, I would say that I have read the thing well over
7 a dozen times and gave it to quite a few of my colleagues
8 and none of them knew what it was really all about.

9 So how the investor could possibly feel that his
10 interests are protected by this disclosure, I wouldn't say.

11 As we are trying to deal with the public, and as
12 we are trying to protect the public, that is the only answer
13 I can give you.

14 MR. BROWNELL: Mr. Froy, I am not conducting this
15 hearing and I am not in a position to request an answer to my
16 question. But I submit that you haven't even attempted to
17 answer it. Maybe you didn't understand it.

18 MR. FROY: I am not a lawyer.

19 MR. BROWNELL: Do not exactly the same principles
20 apply with respect to the sales of Japanese shares as apply to
21 ADR's with respect to the kind of thing you have been talking
22 about?

23 MR. FROY: Mr. Cohen answered this question previous
24 I can only repeat to you that in our opinion the investor --
25 and we will not use the word animal -- who buys a foreign

1 security is a different kind of person from the person who
2 buys an ADE and a differently informed person.

3 This is not based on any contention of mine; it is
4 based on certain years of experience in this business.

5 MR. BROWNELL: I won't attempt to cross-examine on
6 that point. I think his answer speaks for itself.

7 MR. COHEN: Mr. Moxley, it was suggested you might
8 be familiar with the points of view of others trading which
9 have not been expressed thus far.

10 MR. MOXLEY: First, I would like to state that
11 Mr. Froy's statement is incorrect. While it is true that I
12 did discuss the question with the broker community in New
13 York, it was not on the point that Mr. Froy mentioned.

14 I canvassed the community on the question of duplica-
15 tion, which up to now I don't think has been brought to the
16 table directly. So I don't wish to say anything on that
17 right now.

18 MR. COHEN: I understand, then, that you are not
19 in a position to speak to any points of view of traders in
20 these securities with respect to the other problems that
21 Mr. Froy mentioned, apart from the question of duplication?

22 MR. MOXLEY: I would make a general statement, that
23 Mr. Froy and possibly the resolutions passed by the Foreign
24 Securities Committee do not represent the opinion of the
25 community on dealing in foreign securities versus dealing in

1 foreign securities in the form of ADR's.

2 MR. COHEN: Would you expand on that, please?

3 MR. MOXLEY: I think we are getting into philosophy
4 on this question. When you go back to 1955, I think that
5 probably there was a lot to be said that at that time a lot
6 of the conversations might have hinged on then American-held
7 foreign securities. But certainly all of us have witnessed
8 where this American buying of foreign securities has in-
9 creased tremendously.

10 I think it is a matter of opinion, but I believe
11 you would have had that movement even in the absence of ADR's.
12 It is true that ADR's have facilitated this movement inasmuch
13 as it eliminated a lot of the hardships involved in dealing in
14 foreign securities in the back rooms of brokerage houses.

15 Mr. Froy knows -- and I am sure he will agree --
16 that ADR's have eliminated a tremendous amount of back room
17 overhead and back room work. So I get back always that ADR's
18 do not initiate American buying or American interest. ADR's
19 follow it.

20 That is how simple this whole thing is.

21 MR. AUSTIN: I would like to say I endorse those
22 remarks of Mr. Moxley and point out further that the mere
23 existence of ADR's doesn't assure continued trading.

24 I want, for example, to see what happens to the ADR's
25 in this country to see how quickly they are repatriated to

1 Holland.

2 MR. COHEN: We won't get into that problem. I
3 think that is a problem of another character.

4 MR. FROY: May I just say one word more, because I
5 don't want to appear in any way unfair. We had on our Com-
6 mittee originally a position from one or two members who felt
7 that they could not go along with our views on Japanese securi-
8 ties because they happened to be underwriters in the Sony issue

9 We fully agreed that this would prejudice their
10 position as underwriters on one side and our position of
11 issuance on the other side. So I think that answers your
12 question within our small community.

13 MR. COHEN: Mr. Froy, would it be appropriate for
14 you to identify the members of your Committee and the trading
15 houses with which they are associated?

16 MR. FROY: By all means. A position came from Mr.
17 John A. Nevins of Modell, Roland and Stone; and also Jack
18 Block of Bear, Stearns & Co., for reasons which were not given.
19 Those were the two positions.

20 But in all fairness I would also like to state
21 those who were in favor of our resolution. Hugo Van Itallie,
22 partner in Hallgarten & Co. Derek G. Swcock, who is present
23 here, of Carl H. Loeb, Rhoades & Co. Max Halpert of Arnhold,
24 & S. Bleichroeder & Co. Hans Ben, New York Hansentia Corpor-
25 ation. Jerome C. Cuppia, Jr., partner in Merrill Lynch and

1 Company. Marshall S. Mundheim, partner in Hirsch & Company.

2 To be very fair, we invited further to our meeting
3 the following: Albert DeJong of Albert DeJong; Ralph Hilling-
4 ton of Carl Marks & Co. Walter Steiner of White, Feld and
5 Co. Ernest B. Schwarzenback of Smith, Barney, who naturally
6 abstained because he is a chief underwriter of Sony. He was
7 just present to cover our other discussions, and he was ex-
8 tremely helpful in everything which happened.

9 So those were the people present.

10 MR. COHEN: Mr. Stevenson, do you feel impelled
11 to answer any of these remarks now?

12 MR. STEVENSON: I can't answer completely because I
13 didn't attend the Committee meeting. But it does seem to me
14 that the present state of the record -- which held that these
15 gentlemen were opposed in Mr. Froy's opinion only because
16 they were underwriters -- is a little unfair to them.

17 I think they may have had other reasons for opposing.

18 MR. STEVENS: My name is Edwin P. Stevens. Bear,
19 Stearns & Co. is not a member of the underwriting of the Sony
20 issue.

21 MR. GREGG: I am Derek Gregg of Carl H.
22 Loeb, Rhoades & Co. I would like to remind Mr. Froy that,
23 at the particular meeting we are discussing, there was only
24 one member of the Committee in opposition, which was Jack
25 Novins of Modell, Roland and Stone. I think Mr. Froy listed

1 four. He is thinking of a subsequent meeting where the
2 problem concerning Sony trading was discussed. Am I
3 right?

4 MR. FROY: Yes.

5 MR. GREENCOCK: The only opposition was expressed
6 by a member of Modell, Roland and Stone.

7 MR. LOMIS: I wonder if I could ask Mr. Froy one
8 other question. It may be anticipating what may be discussed
9 later.

10 Did the Committee in its consideration of this
11 matter consider not only the impact of these Japanese foreign
12 exchange restrictions, but also the problem that Mr. Cohen
13 referred to earlier, of these rights offerings of the
14 Japanese issues? *Right*

15 MR. FROY: Very much so. As we feel, and as ex-
16 perience has taught us, the only attraction to investing
17 in Japanese securities is you have the benefit of these
18 rights. Otherwise the foreign owner of securities would
19 have dilution of his capital, which naturally was an advantage
20 in a case where there were no ADR's and the individual was
21 doing it for his own account in Japan and he could exercise
22 his rights without our intermediary.

23 Therefore we felt that the Sony issue is a differ-
24 ent type, having fully registered for future rights issues.
25 In the case of these ADR's, you are really extending it to

1 your credit in Japan at the four percent rate against ninety
2 percent which we have to pay otherwise. This, I think, was
3 another consideration.

4 MR. BROWNELL: Mr. Cohen, we are getting into --
5 and I think very properly getting into -- the first question
6 on your list. I think we have pretty well exhausted for the
7 moment, at least, the fourth question.

8 MR. COHEN: The next thing I want to take up is the
9 first question anyway. I want to save the duplication prob-
10 lem for the last, since that might be the most interesting.

11 I am prepared now to deal with the first problem,
12 and that relates to the problems which an investor may encounter
13 when he purchases either a Japanese security or an ADR cer-
14 tificate for a Japanese security in regard to currency re-
15 strictions; restrictions on repatriation of funds, whether it
16 be capital or income; and springing also from the current
17 practice of Japanese industries to make rights offerings on
18 a frequent basis and on a basis which demands some action
19 on the part of the holder to prevent what Mr. Froy has re-
20 ferred to as substantial dilution.

21 Just to maintain the same order, do you wish to speak
22 to that, Mr. Brownell?

23 MR. BROWNELL: I would be glad to speak to that.
24 I start out by stating that I recognize a policy question
25 exists here. That is one that, in line with our previous

policy, we want to discuss with the Commission.

At least, as far as Morgan Guaranty Trust Company is concerned, we don't want to take any action which is not completely consistent with the Commission's ideas of sound policy in this particular area.

I noticed when you referred to those problems you said that the same problems existed both with respect to ADR's and with respect to Japanese stocks generally held in this country. That is generally true. I won't attempt to take time -- because it is now already twelve o'clock -- to review in detail foreign exchange regulations of Japan.

They are set forth, I think, in fairly clear form in the Sony registration statement. But it is, of course, true that Japan, like some other countries, has got foreign exchange regulations. It is also true that Japanese companies have had a practice over a period of many years of making substantial rights offerings at intervals of as frequently as one year or two years; and that those rights offerings are usually made at a price considerably lower than the current market price and in large amounts, the ratios being as high in many cases as one for one.

Let me speak first to the question of the rights offerings. In the case where a ADR is issued and made effective under Form S-12, I see no serious problem, no real policy question, where the company issuing the underlying shares

1 agrees -- as it did in the case of Sony -- that they would
2 register under the 1933 Act any future offerings to share-
3 holders, because in those cases it would be a simple matter
4 for the depositary to forward the literature or the documents
5 pertaining to the rights offer to the holders of ADR's and
6 give them an opportunity to subscribe.

7 In that case the holder of the ADR would be put
8 in the same position as the holder in this country of a
9 Japanese share. If the Commission should come to the con-
10 clusion that it is bad policy for Americans to be allowed to
11 own stocks in Japanese companies, I would think that probably
12 that same policy would have to apply to ADR's.

13 In the case that I have put, however, where the
14 stock that is being offered is registered under the 1933 Act,
15 the holder would be able to protect his rights if he wanted
16 to do so by purchasing them; or he could, if he wanted, sell
17 them.

18 In the cases of these other ADR's, the ones other
19 than Sony which are covered by the existing registration state-
20 ments, the company issuing the underlying shares has not
21 agreed to register any new offerings to the stockholders under
22 the 1933 Act.

23 That would mean the depositaries would not have
24 any means of making those rights available to the holders of
25 the ADR's. That would in turn mean that the rights would

1 have to be sold by the depositary and the proceeds con-⁶³
2 verted into dollars and those dollars would then be distributed
3 to the holders of the ADR's.

4 That is not, of course, an unusual situation with
5 respect to ADR's generally. As you know, it not infrequently
6 happens that foreign companies for whose shares ADR's are
7 outstanding make offerings of new shares to their stock-
8 holders without registering them under the 1933 Act.

9 When those cases come up, the depositary for ADR's
10 sells the rights abroad and converts the proceeds into
11 American dollars and distributes the American dollars to
12 the ADR holder.

13 The difference between that situation and the
14 Japanese situation is really one of degree more than anything
15 else. The rights offerings in Japan are more frequent.
16 The spread between the public offering price and the price
17 at which the rights are offered is greater. In the past,
18 at least, the ratio of the new stock offered to the outstanding
19 stock is a much higher ratio.

20 Therefore, you have the same problem but you have
21 it in much greater degree. You have exactly the same problem --
22 and I keep repeating -- where an individual American stock-
23 holder holds stock in a Japanese company, where the rights
24 that are being offered to him are not registered.

25 There certainly are difficulties in connection with

1 his getting those rights and exercising them, although in
2 some cases the rights may find their way to him and he may
3 go ahead and exercise them by use of the rights.

4 We propose to handle this rights problem, first,
5 by making appropriate disclosures of its existence, not only
6 in the body of the ADR itself but in larger type at the top
7 of the ADR.

8 It may be that the Commission would think that
9 some further disclosure would be required, although I sub-
10 mit that a further disclosure, if not required, might be
11 appropriately imposed on all sales of Japanese stocks as
12 well as sales of ADR's representing Japanese stocks and the
13 issues of ADR's representing Japanese stocks.

14 On the question of repatriating American dollar
15 proceeds from the sale of such rights, the situation is
16 complicated. Since our last meeting down here on this sub-
17 ject, we have concluded that under existing Japanese foreign
18 exchange regulations it is quite feasible.

19 Where the Japanese stock representing the ADR
20 has been held by the depository for more than two years, the
21 rights pertaining to those shares can be sold in the Japanese
22 market and the yen proceeds can be repatriated at the current
23 official exchange rate or the regular exchange rate.

24 Whether or not the shares have been held for two
25 years by the depository, the rights received by the depository

1 on account of shares held by him against ADR's can be
2 sold to a non-resident of Japan. They can be sold here to
3 another American for dollars. ?

4 There are other ways in which dollars can be ob-
5 tained which I shall not take your time to go into. But in
6 brief, the rights pertaining to shares that were held for less
7 than two years can be sold in Japan and the proceeds can be
8 reinvested in certain other types of securities in Japan
9 which can become dollar validated and those securities in
10 turn can be sold in the United States for dollars.

11 The fact that the sale of these rights would be made
12 in different ways, and presumably not all at the same moment of
13 time, would mean that it would be necessary for the depository,
14 in order to distribute equal amounts to each ADR holder, would
15 have to average -- in other words, he might not get exactly
16 the same amount for each right.

17 That is a difference between the position of the
18 man who holds an ADR and the man who might hold the Japanese
19 stock himself -- one of the differences. I want to put it
20 right out on the table.

21 The fact that there would be averaging in such a
22 case would, of course, be disclosed, not only in the body of
23 the ADR but at the top of the ADR itself by appropriate
24 references. There is, Mr. Cohen, a certain degree of averaging
25 in connection with all ADR's -- again it is a matter of degree.

1 In the case of an ordinary ADR for an English stock,
2 where dividends are received in pounds, before they are dis-
3 tributed to the ADR holder they are converted into dollars.
4 Sometimes the block of pounds is sold to one purchaser at
5 one time at a certain rate; and sometimes they might be sold
6 over a period of one, two, or three days at slightly different
7 rates.

8 There is never any attempt to divide the moneys re-
9 ceived among different stockholders in proportion to the
10 dividends that accrued. It would be impossible to do that.

11 So in those cases when dividend checks are sent out
12 to ADR holders, they are sent out on an average basis. The
13 difference is again one of degree because the averaging might
14 involve more averaging in the case of rights sales than in
15 the case of dividend sales.

16 However, we submit that the machinery that we have
17 devised is in accordance with the Act, with a proper dis-
18 closure. It is certainly appropriate to issue an ADR under
19 those circumstances.

20 Now I come back to the policy question. It is true
21 that these large rights are unusual in our experience. It
22 is true that if a man doesn't exercise rights from time to
23 time over a period of years, his original investment will be
24 very much diluted. That certainly is true with respect to
25 any holder of Japanese stocks, and it is certainly true with

1 respect to any holder of ADR's -- that the underlying shares
2 are not covered by an agreement on the part of the issuer
3 that the rights offerings will be registered under the 1933
4 Act.

5 I think the Commission should treat them both the
6 same. If the Commission considers that special rules or
7 regulations or prohibitions will be made in one case, I
8 think they should equally apply to the other.

9 But that is a question of policy really for us to
10 discuss and decide.

11 On the general question of exchange regulations, I
12 have already touched on it. It is true that these exchange
13 regulations impose burdens in the case of both Japanese
14 securities and ADR's that are not present with respect to
15 other ADR's and, for example, British securities.

16 I believe that one of the things the NASD Committee
17 has wanted to do has been to get the Japanese to modify
18 and improve from our point of view those regulations. I
19 am not at all sure that that desire may not have underlain
20 their objection to the effectiveness of the existing ADR's,
21 because I think it may be felt -- I know it is felt by some
22 members of the community -- that the Japanese might be induced
23 to make changes in their regulations if we didn't go ahead
24 with these ADR's. I can only state that as a rumor; I don't
25 vouch for its accuracy.

1 Again, we think that in the case of the ADR's
2 we can cover the matter under the Act by making proper dis-
3 closure of the fact that these exchange regulations exist
4 and that they require certain things and produce certain
5 results.

6 We know of no other way to handle them. I point
7 out that we go further -- propose, to go further -- with
8 respect to such disclosures than under your existing rules
9 and regulations people go in connection with the sale in the
10 market of shares of stock of Japanese companies which are not
11 represented by ADR's.

12 That is a pretty general answer or introduction to
13 this question of the bearing that Japanese companies' policies
14 of issuing rights and Japanese exchange regulations have on the
15 ADR's.

16 MR. COHEN: I think it would be appropriate, follow-
17 ing your discussion, to have Mr. Proy deal with it so we have
18 in one place in the record a discussion of this problem. It
19 is now about 12:15. I am sure we would not be able to conclude
20 this before 1:00 o'clock.

21 I think we probably will have to take an adjournment
22 here and come back in the afternoon. I would like to complete
23 all of our discussion today. There is one question I had,
24 but I will wait for Phil to deal with his statement first.

25 MR. LOOMIS: I just wanted to get in an indication

1 with respect to perhaps the dimensions of this rights question,
2 which frankly has been a source of concern to me. It appears
3 from looking at the Sony registration statement, for example,
4 that between 1953 and 1959, a period of approximately six
5 years, they had five rights offerings, mostly at one for one --
6 some at one and one-half for one -- which increased the out-
7 standing stock from 400,000 shares to 16 million shares.

8 All of the rights offerings were made at par, which
9 was 50 yen -- although at the end of the period, in any event,
10 the market price appears to have been 550 yen. So at least
11 at the end of the period the rights price was about 9 percent
12 of the market price.

13 So this does seem to be a rather unusual, from our
14 viewpoint, magnitude of rights transactions -- at least in the
15 case of this company. Anybody who didn't exercise his rights
16 during that period would have been practically diluted out
17 of the picture.

18 I just wanted to inquire of anyone who is familiar
19 with the matter -- and I am sure a number are -- whether this
20 is a rather typical record, or is this something unusual as
21 far as Japanese --

22 MR. CREWCOCK: It is rather a typical record.

23 MR. COHEN: I want to ask my question, then, because
24 it related directly to this. You made reference to the
25 British system and the General Continental system of making

1 rights offerings. In Britain, as I understand it, there are
2 issued renounceable letters and the market develops in the
3 letters, something akin to the market which develops in this
4 country with respect to rights.

5 I have been led to understand that there is not
6 quite the same situation in Japan. So the problem of actually
7 exercising the rights is more acute. This, I am led to
8 understand, is due to the fact that it is not quite as easy
9 to dispose of rights, nor is it possible to realize, as you
10 can in the United States, in Japan at least the value of the
11 rights.

12 If I am wrong about that, I would like to have the
13 record corrected in any way. I thought we might do that
14 before we adjourn and then after we meet again perhaps Mr.
15 Froy would tell us his understanding of the problems.

16 MR. BROWNELL: Let me again first point out the
17 problem that you raise would exist equally with respect to
18 Japanese shares or ADR's representing Japanese shares.

19 MR. COHEN: Assuming that to be true for the moment,
20 I would like to have --

21 MR. BROWNELL: It is my understanding, although
22 there is a difference of the kind that you indicate, that
23 there is a distinction in the market for rights to purchase
24 shares in Japanese companies and rights in this company repre-
25 sented by a sort of warrants or rights in Great Britain.

1 I am informed, however, that there is in these
2 cases an adequate market for the rights; and certainly the
3 depository would be able to do at least as well as any
4 individual holder of Japanese shares.

5 If there is objection on the score that we made,
6 then you ought to do something about letting Americans buy
7 Japanese shares.

8 MR. COHEN: Just to expand my question, it is my
9 understanding that the over-the-counter market in Japan is
10 not quite the same type of market that we have here; that
11 most securities are traded on the exchange; that the ex-
12 changes have not yet adopted the practice of permitting trad-
13 ing in the rights.

14 In consequence, there is not quite as good --
15 if there is any -- market for rights in which fair values
16 can be realized.

17 If you can speak to this, I would appreciate it;
18 or if you cannot, we will wait until Mr. Froy speaks to it
19 this afternoon.

20 MR. BROWNELL: I can only answer it as I have
21 answered it at this time.

22 MR. COHEN: Perhaps Mr. Stevenson, who has just gone
23 through someing of a baptism in this area, can contribute
24 some light to the subject.

25 MR. STEVENSON: I think there is some background

1 that is useful in this connection from a legal standp oint.
2 You cannot transfer rights if you are a Japanese resident.
3 However, the Japanese foreign investment law allows the
4 companies to consent to the transfer and sale of rights
5 in the case of foreign stockholders.

6 Accordingly, as far as Japanese holders are con-
7 cerned, they have not been in position to dispose of their
8 rights. In the case of companies that have an appreciable
9 number of foreign stockholders, they have usually given this
10 consent.

11 However, it is of course true that, for the reasons
12 you yourself mentioned, in most instances there is a prefer-
13 ence for exercise rather than sale even in the case of
14 foreign stockholders.

15 While there is no active market in rights in Japan
16 in the sense that they are not quoted on the stock exchange
17 so that you can't actually get a stock exchange quotation,
18 I have been advised that in disposing of rights -- at least
19 the one situation that I knew something about in the case of
20 Sony -- because some of the rights there were disposed of,
21 people did get a price that was reasonably related to the
22 market differential.

23 The extent to which they have been able to achieve
24 this on a more general basis is something that I think could
25 only be determined by knowing what the history of all the

1 firms which have handled the sale of rights might be.

2 I don't have that information. But there is, as
3 I understand it, a fairly active ~~market~~ market in
4 Japan which would afford you some criterion for determination
5 whether your price was fair or not.

6 MR. COHEN: This is a matter that goes to the crux
7 of the disclosure problem, or one of the disclosure problems.
8 It is a matter as to which we would like to be exposed fully
9 to the extent that we can, either today or at some other time.

10 I am sure some of you fellows got up early this morn-
11 ing to get here and you may be hungry. This may be a good
12 time to adjourn. We have a number of other things to talk
13 about. I don't know how long it will take. Can we come
14 back at two o'clock? Is that agreeable to everyone?

15 Some of you have appointments with me for this
16 afternoon. We will just move the hours down a little further
17 on the clock.

18 (Whereupon, at 12:25 p.m., the conference recessed,
19 to reconvene at 2:00 p.m. of the same day.)
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Midler

AFTERNOON SESSION

(2:00 p.m.)

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3 MR. COHEN: Before I ask Mr. Froy to deal
4 with this problem, I think that in order to have a complete
5 record, Mr. Brownell, I will ask you whether there is any-
6 thing more you want to add to what you said this morning
7 and whether Mr. Stevenson has anything further to add.

8 MR. BROWNELL: I would like to, after Mr. Froy
9 has spoken, if I may.

10 MR. COHEN: All right. Mr. Froy, I will ask you
11 to deal with this problem, just the way you think best.
12 You need not confine yourself to the frame-work in which
13 Mr. Brownell put it although I would like you to supplement,
14 modify or distinguish any of the remarks he made with
15 respect to the several matters he discussed: The currency
16 restrictions; repatriation of funds; and the rights offering
17 procedures in Japan, as well as the markets for rights and
18 similar matters, and I have particular reference to the
19 reference Mr. Stevenson made in the case of Sony; as he
20 understands, there was not much difficulty in taking
21 care of the rights which were offered as a result of the
22 U.S. offering. I mean, offered in Japan.

23 MR. FROY: Before I answer this, I may say I
24 feel very much better now because Mr. Brownell was kind
25 enough to tell me that we are both here on business, so

1 I feel less accused than I was before.

2 May I start with the end of your remarks and that
3 is the question of rights offering and the facility of
4 disposing of rights in Japan, and Sony in particular.

5 I will start with Sony. I believe that Mr. Stevenson
6 is correct, that there is not an open market in rights in
7 any security in Japan -- open market, I mean. There is
8 neither a stock exchange quotation which could be checked
9 nor a free over-the-counter market.

10 In the case of Sony, I have been led to believe
11 that the specialist in Sony who is also generally the buyer
12 of A.D.R.'s, is in Immure securities -- one of the
13 major underwriters of this latest issue.

14 I have no means of checking if the price which
15 the banks achieve for the rights of the A.D.R. holders
16 is the best one obtainable if it goes to a specialist who
17 himself has an interest in the security. That is a very
18 serious point and the next point which is really worrisome
19 to the N.A.S.D. is that through dealing in rights, and try-
20 ing to discover the best market, the banks are getting
21 again, more and more into the securities business.

22 I believe they have not the same facilities of
23 checking a market via bank correspondence that we have
24 with the know-how, which the City of New York has acquired
25 over many years of international trading. It would be

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very difficult to disclose to our customers that the proceeds of these rights may very much vary in price on account of the rate. First of all, you will not receive immediately, on the sale of your rights, the official yen rate that is clear under the existing foreign exchange restrictions. You are either blocked with your yen as long as you are blocked with your underlying securities, or you could try to sell these proceeds in the New York over-the-counter market to some kind of philanthropic association who would like to be locked up in yen from any period from 23 months to one month -- whatever the A.D.R.'s have to run.

Well, maybe many of us have money to waste but I still think you will find it very difficult to call this a freely convertible currency.

Mr. Grecco who has also recently returned from Tokyo has made a very close study of the foreign exchange restrictions of Japan and I think he will be able to explain our disagreement with Mr. Stevenson's statement and with Mr. Brownell's statement better than I can; so I will call on him.

MR. COHEN: Have you identified yourself for the record?

MR. GREWCOCK: Derek Grecco.

We feel that the exchange regulations governing the trading of securities are extremely complex. In fact,

1 there are five kinds of yen. This is all covered in the
2 prospectus of course.

3 I would like to spell it out here.

4 There are five kinds of yen and we must consider
5 four of them, whenever we are trading in securities or
6 rights.

7 MR. COHEN: Some of the people here are having
8 difficulty hearing you. Would you speak up, please?

9 MR. GREWCOCK: First of all, is the Non-
10 resident yen. This can be used -- if I may read from
11 notes here -- this can be used to purchase securities
12 by non-residents; however, the proceeds from the sale
13 of equities are not convertible at the free rate -- which I will
14 come to in a minute -- but after a two year deferment period,
15 although dividends and interest may be remitted at the free
16 rate. Non-resident yen is freely transferable between non-
17 residents against payment in foreign currency; however, it
18 can only be converted at the free rate by purchasing corporate
19 bonds with a maturity of not less than two years and holding
20 them to maturity. It follows therefore, that the holder of
21 securities purchased with non-resident yen is at a dis-
22 advantage against the purchaser in free yen, because he does
23 not have the two year waiting period, at the end of which
24 time he can get his proceeds out at the freely convertible
25 rate, which is three-sixty or various percentage on the

side of three-sixty.

Secondly, yen with deferred convertibility. This is not an official description but a term arrived at to describe yen arising from the proceeds of sale of securities originally purchased with free yen and not held for the full deferment period of two years. Proceeds of sales of securities not held for a full two year deferment period must be reinvested within four months.

This has some disadvantage in that yen with deferred convertible loses its convertibility if it is not used in practice within four months.

The rule says one month; in practice you can use up to four months.

After the expiration of four months, the item becomes totally blocked, or you have to transfer it to a non-resident account, which is the first kind of yen we discussed.

Thirdly, this free yen, which can be purchased against dollars and several other currencies, which is permitted to fluctuate.

When I was in Japan, it was 1/2 of one percent; on either side of 360 per \$1 -- I think there is a little change there. 3/4's of one percent on the other side of 360.

Then the other kind of yen with which we must

ourselves is yen arising from the sale of rights.

Proceeds of the sale of rights are subject to the same regulations as the proceeds of sale of the shares from which such rights were derived with the treaty, except that such proceeds may be held in a foreign investors deposit account in cash pending repatriation at the expiration of the two-year deferment period on the underlying shares.

It therefore differs from free yen, which is freely convertible, or yen with deferred convertibility which has a four-month time lag.

Therefore, we feel that these regulations are extremely complex and militate against the issuance of A.D.R.'s at this time.

MR. COHEN: Thank you.

Mr. Froy, do you want to add to that?

MR. FROY: Well, these regulations as read out to you, are the result of probably studying this for many, many weeks, and bringing it down to a point where a few professionals can understand what we are talking about, but I should think the broad public is being -- forgive me -- misled if A.D.R. is in existence, where the public might have the feeling that all problems have been ironed out for them by the banks who are, to their mind, the issuer of these A.D.R.s, even if we know they are not the issuers of A.D.R.s and it is really difficult

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1 to persuade the public that they have to study the prospectus
2 of the size of the Sony prospectus, more or less until
3 they know what they are getting. So why should we be
4 forced into making a market in something where we feel we
5 cannot protect or disclose efficiently to the public, the
6 risk they are running and what should the interest of the
7 banks be, to foster this business on to us, which we do not
8 want. When we want their facilities, we ask for them; we
9 have done so before. They were very helpful in issuing it.
10 They never regretted it because their income has profited
11 from it.

12 MR. COHEN: Without appearing to take one position
13 or another, Mr. Floy, I think you indicated this morning
14 that you were in a position to make the necessary dis-
15 closures to the individuals who perhaps have been accustomed
16 to trading in foreign issues.

17 I take it you mean this type of disclosure
18 which has now been explained in somewhat summary form, and
19 the type of disclosure that you would make to your customers.
20 Is that right?

21 MR. FROY: Yes.

22 MR. COHEN: Is it not possible to develop
23 in written form such disclosures and could such disclosures
24 accompany any offering document in connection with the
25 A.D.R. arrangement to the same extent that you would make

1 the disclosures informally or formally to your private
2 customers?

3 MR. FROY: Mr. Cohen, one of our competitor
4 firms has traded a few weeks ago with a firm on the Coast,
5 in Japanese A.D.R.s and they have read a similar statement
6 to them prior to dealing, and have subsequently sent
7 their contract to this customer with a stamp attached, cover-
8 ing these regulations, and asking them to return the contract
9 copy with their signature as to the agreement that they have
10 read these regulations.

11 The customer has returned both contracts -- the
12 original and the copy -- and he said he misunderstood those
13 regulations and therefore, he would like to cry off the
14 bargain because he has been misinformed, and I have no way
15 of supplying every one of my trades with a microphone,
16 taking down what has been said on both sides, and I think
17 the average dealer will be in a similar position.

18 MR. COHEN: I am not sure I fully appreciate that.
19 I take it you are now saying, Mr. Froy, that you might
20 make certain trades in Japanese securities, ignoring
21 A.D.R.s for the moment?

22 MR. FROY: That is right.

23 MR. COHEN: I took it from what you said
24 earlier in connection with such trading activities,
25 you would make disclosure to your customer?

1 MR. FROY: Well, there is one difference.

2 My only business now is to execute orders.

3 The customer calls me up and says, "Do you have an opinion?"
4 I say, "I like them but you know the risk" and this man
5 will understand these risks perfectly well because he is
6 giving me an order; shares are being placed in his open account
7 in Japan. That ends that end of it.

8 Here we have to go further. We have discussed before,
9 our rights. He is losing benefit of those rights, even if he
10 gets a certain amount of cash for it.

11 MR. COHEN: I am not going to quarrel with what
12 you say, Mr. Froy. How do you know and how does the man in
13 Loeb Rhodes know this customer who calls up, understands
14 this intricacy which I am frank to say, a great many of
15 us do not.

16 MR. FROY: This is generally business which
17 has not been canvassed by us but it is coming to us on
18 account of a person who understands something about inter-
19 national business. We are in a different position to
20 explain to them what has happened, if we make a trading
21 market, which is our duty as broker-dealers.

22 MR. COHEN: Do I understand you to say that your
23 activity is limited to filling orders? You don't solicit
24 any business in this area at all?

25 MR. FROY: At the present time, in Japanese

1 securities, this is 90 percent true.

2 MR. COHEN: And this is wholly voluntary business?
3 It is not generated by anyone in the trading fraternity?

4 MR. FROY: Very little, except the Japanese
5 brokers who advertise on a really large scale.

6 MR. COHEN: Do you mean the Japanese brokers
7 in the United States?

8 MR. FROY: Right.

9 MR. COHEN: So they are soliciting business in
10 this area?

11 MR. FROY: Yes.

12 How much they disclose, in spite of the fact
13 they are members of the NASD, I don't know.

14 MR. COHEN: I was going to raise that question;
15 whether you, in your official capacity, have interested
16 yourself in this problem.

17 MR. FROY: I will say they have done so little
18 business here that the Ministry of Finance is getting
19 extremely worried as to whether they should not close the
20 office, because there are so many expenses and they have
21 not produced any business.

22 MR. COHEN: I take it then from what you say
23 that the NASD as such, has not reached the point where
24 it is prepared to issue any rulings, or rules, with respect
25 to the nature, the quantity and the quality of disclosures

1 that should be made in connection with trading in Japanese
2 securities?

3 MR. FROY: Well, we have not because so far, this
4 Committee has voted that they do not wish to have Japanese
5 A.D.R.s in existence because they feel that they could not
6 comply with the requirements which I expect.

7 MR. COHEN: You make a distinction between the
8 A.D.R.s for Japanese security and the Japanese securities
9 themselves.

10 MR. FROY: Very strongly.

11 MR. LOOMIS: If I understand you, just to summarize
12 a little, you were saying that the existing trading in
13 Japanese securities is mostly done -- aside from perhaps
14 the Japanese firms -- in response to unsolicited offers
15 by people who are fairly knowledgeable and if not in
16 details of Japanese restrictions, in international finance.

17 MR. FROY: Right.

18 MR. LOOMIS: So that you can explain to them what
19 these problems are and they will understand the language
20 you are talking, in any event, but that if you got Japanese
21 A.D.R.s then you would be expected to make a trading
22 market which is their usually fairly rapid telephone type
23 operation, in and among dealers and the customers, and you
24 don't think it feasible to make these disclosures in the
25 context of that market, and that in view of the identity

1 and experience that people who might be in it would have?

2 MR. FROY: That is right.

3 MR. COHEN: There is one thing that you failed
4 to add to what Mr. Froy said. I wanted to be sure I under-
5 stood that.

6 I understood Mr. Froy to say that when someone
7 calls him he inquires whether the caller understands the
8 risks. I did not understand that on the telephone, he undertakes
9 to explain the risks. I would like to know which is the
10 correct understanding of what you say?

11 MR. FROY: We explain the risks attached to it
12 and we also draw his attention that we would not be able,
13 as brokers, to hold the securities for him, that we would
14 open an account and have these securities delivered to the
15 National City Bank in Tokyo. From that moment on, he is
16 no his own.

17 MR. COHEN: Let me carry this one step further.

18 Assuming that the banks and others in the A.D.R.
19 arrangement would devise a procedure whereby the investor
20 would be appraised of these rights, in some form that
21 you would consider suitable and intelligible.

22 Would you have the same concern that you now
23 expressed?

24 MR. FROY: Well, I should think that it is easier
25 to explain the situation to an investigator than to the

1 ordinary trader on the telephone to whom you are expected
2 to make similar disclosure, and an out-of-town broker, if
3 he calls me up, I cannot say, "If I buy these from you, I
4 must know how old these A.D.R.'s are, because it depends
5 on my price -- if they are six months or eight months. If
6 I sell them to you, you must understand these regulations."

7 MR. COHEN: I was just trying to underline the point
8 you made in response to Mr. Loomis' question. Essentially
9 what you are saying is that from the point of view of face-to-
10 face dealings with a customer that you know and to whom
11 you can make the necessary explanations, that you have
12 less concern than if a market is to be created here, which
13 is essentially a telephone market of the usual variety?

14 MR. FROY: Right.

15 And I would like to refer to another remark from
16 Mr. Brownell, in which he said they intend to show clearly
17 on the A.D.R. how rights are being dealt with and that
18 they are probably disposed of at an average price, as we
19 also do in the case of other securities.

20 I wonder why a similar disclosure is not also
21 shown on the British A.D.R.'s where I am sure a similar
22 sale is taking place, on average price, and why should
23 we suddenly have the facility on Japanese A.D.R.'s?

24 MR. BROWNELL: The answer is very simple.

25 It happened very infrequently and the market is such,

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1 that the average results in such small differences, as not
2 to make it a matter of reports.

3 MR. FROY: I would say, if you just take the present
4 time, you said that in Britain these right issues are traded
5 on an allotment basis, which may easily be traded for three
6 weeks. Say for instance, you would sell the first lot today;
7 the next lot in a week's time and South Africa decides
8 to tear themselves away from the British Empire, and you only
9 get half the rate for the balance.

10 Won't you owe an explanation to your patrons?

11 MR. BROWELL: The practice is not three weeks.
12 It is a period of a few days.

13 MR. FROY: You see why the banks are getting
14 into a business which is out of their department. If we
15 have to dispose of rights to customers in any shape or form
16 in the foreign country, if we live there over a 30-day
17 period, we will give instruction to a broker to sell a thirtieth
18 part every day to be fully covered and protect the customer's
19 interest.

20 MR. COHEN: There are a few things I would like
21 to say.

22 One, Mr. Froy has anticipated a question I was
23 going to raise in respect to A.D.R.'s of non-Japanese
24 variety. I think the South African situation would highlight
25 a problem.

1
2 Before I forget again, I did not intend, at
3 least so far as I was concerned to raise any specters
4 of problems that might arise under the Banking Act of
5 1933 with respect to the activities of the banks here in
6 the distribution of security. This is a matter that would
7 have to be dealt with in another forum and I don't intend
8 to get into that but getting back to the other point, am
9 I correct that when the South African State broke away from
10 Great Britain, there were certain currency restrictions
11 placed into effect, and I am not aware that any of the
12 banks issuing A.D.R.'s undertook to advise those to whom
13 A.D.R.'s might be issued thereafter, in the few situations
14 that do exist, with respect to this matter -- or am I wrong
15 about it?

16 MR. AUSTIN: You are right, I think.

17 MR. CARR: You are right.

18 MR. COHEN: Let me broaden the question. I don't
19 know to what extent there are other A.D.R.'s in existence,
20 where there is a restriction or a problem of restrictions,
21 with greater or lesser extent, similar to the ones that
22 exist as a result of the South African situation or the
23 Japanese situation.

24 I wonder if someone can enlighten me on that?

25 I am just trying to understand the scope of
the problem.

1 MR. CARR: You are talking about other currency
2 restrictions. Great Britain? Australia?

3 MR. COHEN: I meant something beyond the normal
4 situation that we are all familiar with; the Sterling
5 situation. That sort of thing. I meant something that goes
6 beyond that which is in existence in South Africa and of the
7 kind exemplified by the Japanese situation.

8 Now, does anybody in the N.A.S.D. group wish to add
9 anything further before Mr. Bronnell gets his opportunity
10 to respond?

11 MR. FROY: Well, I think we have covered it.

12 I have given you enough reasons why we feel that
13 we could not maintain an orderly market here, and comply
14 with the requirement of the N.A.S.D. and the protection of
15 the public in advance of trading.

16 MR. COHEN: Mr. Bronnell?

17 MR. BRONNELL: Mr. Cohen, I feel, I admit, these
18 Japanese foreign exchange regulations involve complications
19 in the Japanese A.D.R. picture.

20 It is one of the reasons we are here.

21 I don't deny that there is a policy question
22 involved. I submit that the policy question is one that
23 can be properly resolved under the Act if a proper dis-
24 closure is made. I repeat that.

25 The Morgan Guarantee Trust Company of

1 New York is prepared to make any disclosure that the
2 Commission or the staff urges or recommends on this
3 particular subject, as we always have been in the past,
4 and we have suggestions to make ourselves. I do not really
5 gather a clear answer from Mr. Froy to the question that
6 you asked him.

7 He says, as I understand it, that he would
8 find it impossible to explain the foreign exchange regula-
9 tions and the complications relating to rights, to a man
10 who came to him and said, "I would like to buy an A.D.R."
11 He says, if I understood him correctly, that if that same
12 man comes in and says, "I want to buy 100 shares of
13 Japanese stock" that he would have little difficulty in
14 explaining the same kind of thing to him. He made differ-
15 ing answers. One of the answers was that he would say to
16 the man who wanted to buy Japanese stock, "Well, you are
17 a sophisticated investor. You know what the risks are.
18 All right. Send me a check. I will buy 100 shares for
19 you."

20 I submit that is not a full disclosure; whether
21 or not the man is a sophisticated buyer. I submit that
22 the problem in connection with the sale of shares of
23 Japanese stock is exactly the same as it is in connection
24 with the issuance of the A.D.R.'s or the sale of A.D.R.'s.

25 Now, if Mr. Froy --

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MR. COHEN: Excuse me, Mr. Brownell. May I interrupt you.

I don't attempt to speak for Mr. Froy. He can do that better himself but I think as we clarify the position Mr. Froy expressed, it was that whether A.D.R. or securities, presumably, if you were dealing face to face, he could make explanations. The difficulty of explanations would in some degree depend on the sophistication of the customer; but he could contend with that.

I think what he was saying was that once you introduced A.D.R. and facilitate trading, you are going to create the type of trading that exists in over-the-counter markets in the United States where trades are made over the telephone and he says this sort of trading does not lend itself to the type of disclosure which requires precise and careful explanation that he can make face to face. That, I understand to be his point.

Handwritten:
H. Brownell
H. Brownell

MR. BROWNELL: Yes, I hesitate to question Mr. Brownell and also the Commission in that particular area, except to say this. I would like a lot of proof before I accepted the fact that everyone who acquired an A.D.R. is in the position of an unsophisticated man dealing very rapidly over-the-counter, whereas the man who choose to purchase a hundred shares of Japanese stock without buying an A.D.R. was in an entirely different category,

1 therefore, could be handled more readily and more
2 easily.

3 MR. COHEN: I just want to say that I was attempting
4 to rephrase Mr. Froy's statement.

5 I did not purport to make any statement on behalf
6 of the Commission, of the staff, or on my own behalf.

7 MR. BROWNELL: I am sure of that.

8 MR. LOOMIS: Also to further carry on again
9 with the point I think Mr. Froy was making, and for my
10 information, I understood him to indicate that at the
11 present time at least, with regard to the Japanese securities
12 themselves, there is not the usual type of over-the-counter
13 market that exists in the United States in trading in, say,
14 bank stocks; but that with the development of A.D.R., there
15 would be expected to be that kind of a market, and that
16 is where a part of the problem would arise?

17 MR. BROWNELL: That is what Mr. Froy said,
18 Mr. Loomis, to a certain extent. I think he indicated
19 that but I think that would be a very bad bomb on which
20 this Commission might rest the distinction because you
21 heard the figure this morning, for the number of holders
22 of Japanese shares of these different countries in the
23 United States; I think it is a matter of common knowledge,
24 the interest in them is increasing steadily all the time.
25 We know at the moment, there is only one A.D.R. set up --

1 to wit, the Sony one -- that takes care of it and I submit that
2 it would be very ill advised for the Commission to say, in case
3 of A.D.R., we think such and such a disclosure is essential
4 but we will impose no restrictions at all in connection
5 with the sale of Japanese stocks. I think if you are going
6 to impose any regulations, and you may well see fit to do
7 so, they should apply not only to the issuance and sale of
8 A.D.R.'s but they should apply to stocks of all Japanese
9 companies, and if you drew up such a regulation, I am sure
10 Morgan Guarantee and I am sure these other banks also, they
11 can speak for themselves, will be more than glad to comply
12 with it.

13 MR. COHEN: I am coming back to this point now. I
14 want to take up Mr. Froy's point.

15 If I understood your position correctly, as I
16 expressed it, Mr. Froy, let me ask you first whether I did
17 express it correctly?

18 MR. FROY: You did. Absolutely.

19 MR. COHEN: If that is correct, if you would agree
20 with me if there is a telephone market in the Japanese
21 securities of the kind we have described, then you would
22 express the same concern with respect to that type of
23 trading as you would with respect to A.D.R.?

24 MR. FROY: Indeed, I would. It could not
25 develop.

1 MR. LOOMIS: Now, the next question is that I think
2 I will ask you to inform me -- the N.A.S.D. -- whether or not
3 there are such markets.

4 MR. PROY: In Japan?

5 MR. LOOMIS: In Japanese securities in the
6 United States. In other words, is there trading beyond
7 the confines of the New York market, and how is that market
8 conducted in New York City, because I take it from your own
9 position, you would have difficulty if there is a type of
10 inside market developing in Japanese securities.

11 MR. PROY: There is a market all over the United
12 States in Japanese securities, on an order basis in most
13 cases. I only know of one firm in New York City who makes
14 a market in a few Japanese securities, on a very, very narrow
15 scale. I would classify these people rather as brokers'
16 brokers and they have spent many years before anybody has
17 thought of A.D.R.'s in explaining the Japanese currency
18 regulations to these correspondents of theirs, because
19 the Japanese regulations were more stringent but they have
20 really not changed much except as it has been shown.

21 So I think you have a very large interest in
22 Japanese securities in Hawaii, on the coast, the West Coast,
23 and to a small extent in New York, but in actual trading,
24 apart from Sony, you would not call it an existing over-
25 the-counter market.

1 MR. COHEN: Let's take Hawaii. I have been led to
2 understand that there is very substantial and active market
3 in Japanese securities in Hawaii.

4 Are you familiar with that?

5 MR. FROY: Yes. I have just been there for that
6 purpose.

7 MR. LOOMIS: That is a fairly broad market --
8 Hawaii?

9 MR. FROY: It is purely based on orders which are
10 passed through three Japanese broker houses which have
11 branch offices, I think, or their own offices, in Hawaii.
12 The banks don't trade and the brokers pass the orders to
13 the Japanese brokers. I have not found a trading market
14 of any kind.

15 MR. COHEN: What about the West Coast? California?

16 MR. FROY: Very small.

17 MR. LOOMIS: With further reference to Hawaii, I
18 would like to go into that. I have heard from time to time
19 that there are small brokers, often of Japanese extraction,
20 who offer Japanese securities to their customers who
21 again may be people of Japanese extraction and that this
22 is fairly active. It is on the selling end.

23 MR. FROY: Well, I am afraid this is a lower type
24 of animal than I have covered.

25 MR. BROWNELL: I submit, Mr. Cohen, if I may, that

1 even taking everything Mr. Froy says as accurate, and I
2 am not questioning his intent to be completely accurate, any
3 moment, your sophisticated market in Japanese stocks could
4 change. We know the interest is mounting; if what he said
5 is correct, I don't know that you ought to rely on the fact
6 that it is only unsolicited orders that come in when
7 Japanese stocks are bought, but where there are A.D.R.'s they
8 are always bound to be solicited and perhaps he would suggest
9 high pressure or something like that.

10 I think you better draw some kind of a rule, if
11 you are as anxious about disclosures as he is, in the case
12 of A.D.R.'s which would be available if the temper that
13 he describes, happens to change over night. You are getting
14 there very quickly. Then we will follow the same rule
15 on A.D.R.'s.

16 MR. FROY: We should have a school for dealers
17 in Japanese securities, where they could be trained in
18 Japanese foreign exchange regulations, to relieve the
19 banks of their responsibility in our desire for protection
20 to the public.

21 MR. CONN: Do any of you gentlemen at this
22 end of the table dare to join the fray?

23 MR. CARR: We have given a great deal of thought
24 to the views expressed by the representatives, and
25 resolutions passed there, at their various meetings.

1 It is our feeling that the Japanese exchange
2 regulations are so complicated that it is almost impossible
3 to explain them in a short way to the type of investor
4 who would be attracted, presumably, to Japanese securities
5 by the A.D.R. procedure.

6 Take the Sony prospectus. I assume that that --
7 I am sure that it is the product of very able minds; not
8 only of the banks and the underwriters and the Securities
9 and Exchange Commission, but I will be darned if I can
10 understand it and a lot of people who are a lot more
11 sophisticated than I, find it almost impossible to understand.

12 How are you going to, in a short way, explain
13 that to the average A.D.R. investor? *change*
back

14 Our feeling would be -- as a part of the machinery,
15 -- in connection with the A.D.R.'s that it would be much
16 better to wait until the Japanese have modified their
17 restrictions so as to give us what you might call a real
18 security yen, before trading, as is allowed in the
19 Japanese A.D.R.'s.

20 MR. BROWNELL: May I speak to that, Mr. Cohen?

21 MR. COHEN: If I may just say one word before --
22 that I don't intend this to be any criticism for the
23 explanation given of the Sony prospectus. I must disallow,
24 completely, any claim to authorship by the Securities and
25 Exchange Commission.

1 MR. CARR: You must have looked at it.

2 MR. BRONNELL: We are getting into another policy
3 question. To what extent should disclosures be made in
4 connection with the purchase and sale in this country of
5 stocks of foreign companies which are not subject to the
6 '33 Act. That is the whole question -- the foreign exchange
7 Government regulations, and so on.

8 You can say, very easily, that the buyers would
9 be advised that there are foreign currency regulations
10 which may materially and perhaps adversely effect his
11 interest but they change of course, from month to month,
12 sometimes from week to week.

13 I would hesitate to see the Commission adopt
14 a principle that was necessary to set forth in great
15 detail all of these foreign exchange regulations because
16 I think you would make almost impossible in some
17 cases, the normal transactions involved in securities.

18 I am mindful of the fact that it has been said
19 to be the policy of certain divisions of our government --
20 I think at one time subscribed to by the Securities and
21 Exchange Commission -- that we should not unduly restrict
22 investments by Americans in foreign companies because it
23 was one of the ways in which, without using Government
24 funds, we would be affording the assistance of the
25 American dollars in foreign areas.

1 I think that purchasers should be
2 given fair notice that certain situations exist but when
3 you talk about long and complicated pages of prospectus
4 memoranda, I don't think they are necessary. I don't think
5 they are necessary in connection with the sales of securities
6 that are not subject to the '33 Act.

7 MR. COHEN: Well, you raised some large philosophical
8 problems, Mr. Brownell, as well as legal problems. If
9 everybody wants to make the plane at 4:00^{o'clock,} we will put those
10 aside for the moment.

11 MR. BROWNELL: Please do.

12 MR. COHEN: But I will only say this. That there
13 is no desire on the part of the Securities and Exchange
14 Commission to impede the capital market, the securities
15 markets, but we do have a responsibility and this is the
16 only time we are criticized, when we fail to recognize
17 that responsibility to assure the investor that he gets
18 the information he needs when he is entitled to it.

19 We also have a notion here at the Securities
20 and Exchange Commission, that the professional people
21 in the business -- brokers and dealers -- have a somewhat
22 higher responsibility than a man dealing at arm's length
23 with his fellow man.

24 It is in this context that we have the notion,
25 perhaps not fully developed, that there is a duty, parti-

cularly in context such as this. Now, we may quarrel about the extent, the nature of the disclosure, but I don't think you will find anybody on this side of the table, who could agree that disclosures are not necessary in this type of situation.

MR. GROWHELL: You will find everyone on this side of the table concurring with you.

MR. COHEN: And there is concern here, particularly in the light of all these gentlemen said, whether or not we made a mistake in the Sony case, and whether or not it is possible to provide adequate disclosures in this situation, in the present context.

Now, in the Sony situation, one of the main problems was obviated. This has not taken place in any other situation that I am aware of.

MR. BROWELL: You refer to the rights question?

MR. COHEN: That is right.

Phil, do you want to get into this philosophical discussion at all?

MR. LOOMIS: Not particularly, except to say that there is of course, a problem, but I have the impression that it is a somewhat different problem than the one we are here primarily concerned with, as far as the combination effect of the Japanese currency restrictions and the Japanese practices with respect to rights which inter-

1 look to a considerable degree, particularly I think, with
2 respect to where you don't have the Sony solution and
3 therefore, an investor who acquires rights, I suppose,
4 will have to sell them and once he sells them he comes
5 up against the same currency restrictions.

6 MR. COHEN: Isn't it true -- I guess Mr. Froy said
7 this -- I want to be sure that I understand it, anyway.

8 The suggestion was made that in the Sony case,
9 the principal underwriter -- one of the principal underwriters
10 -- Inmure Securities Company, I think it was -- of course
11 had an interest in assuring some sort of market for the
12 rights in the context of the offering made in the United
13 States; an interest which might not exist in any other
14 situation which is not the Sony character. That is, where
15 there has not been a registration statement filed, and
16 effective under the Securities Act.

17 Is that a fair statement, Mr. Brownell?

18 MR. BROWNELL: I would rather let Mr. Stevenson
19 answer that one. I think it is a fair statement. I am not
20 sure.

21 MR. STEVENSON: Certainly, there was an interest
22 in that case. I am not sure I can answer the negative. I
23 would assume that the Japanese securities firms are interested
24 in having an orderly market in any Japanese security
25 in which they are trading. I think the question that has

1 been raised is a question of ability to do that, but I
2 certainly think --

3 MR. COHEN: Maybe we can deal with it by asking
4 Mr. Froy what has been the experience of investors, to the
5 extent he knows, who hold Japanese securities with respect
6 to these rights offerings?

7 MR. FROY: I would not know. On the day the
8 people bought their securities, they were handed over to
9 them and they were kept at the National City Bank; whatever
10 instructions they have given since that time to the National
11 City Bank is out of our control but I believe they have had
12 no regrets that they bought these shares when they bought
13 them.

14 MR. COHEN: I wonder if the National City Bank
15 can tell us what happened?

16 MR. ROBERTSON: If I may talk, the shares
17 were placed in the bank's custody for the customer, as
18 distinguished from this A.D.R. arrangement.

19 MR. COHEN: I don't want to create any embarrassing
20 incident. I will withdraw the question.

21 MR. STEVENSON: I wonder if I can say one word.
22 We discussed Sony a good deal. I think the task of a
23 pioneer, particularly in the case of the first offering
24 to Japanese securities, is a difficult one, but I do
25 think that there are some areas of difference that are

1 apparently before us here, which are not really differences.
2 I think that on this disclosure question there have been,
3 really, two questions raised. One is the question of the
4 type of disclosure that is going to be required in the case
5 of the continuing Japanese A.D.R.'s.

6 The other is the question of disclosures that were
7 made in the Sony prospectus and I think that all of us that
8 had anything to do with Japan, would certainly hope that
9 the exchange restrictions can be further simplified.

10 I think that would be something that is in every-
11 one's interest. Certainly, if that can be achieved, it
12 would make for a much more understandable situation.

13 As to the exchange regulations at the present
14 time, I don't believe that any of these statements are
15 intended to say that what was included in Sony was not
16 accurate.

17 I think we should point out that it was reviewed
18 by the Ministry of Finance and by counsel in Japan, and that
19 to attempt to simplify this much more would obviously, create
20 problems.

21 I don't think that my disagreement with Mr. Froy --
22 I am not sure that we have so much disagreement on this
23 point -- but I know that his Committee, the minutes that
24 he read to you approve going ahead, as far as the Sony
25 transaction was concerned, and there was no dispute, at

1 least as to the shares, that were being covered by the S-1
2 registration statement, so I don't think there is any
3 issue before us on that. We are not in disagreement on
4 that, are we, Mr. Froy?

5 MR. FROY: On this particular issue, the customer
6 who acquires new Sony shares should be supplied with
7 a prospectus; a full prospectus.

8 MR. STEVENSON: Yes.

9 MR. FROY: If, in the case of the S-12, -- where
10 also, Sony should -- this may have been omitted in some
11 cases by the brokers if they think they have substituted
12 this disclosure in handing this A.D.H., I am afraid they
13 have been very much missing their duty, as far as disclosure.

14 MR. STEVENSON: You were not questioning
15 adequacy of the disclosure in the full prospectus?

16 MR. FROY: As you know, we had a few discussions
17 on it. You were kind enough to make those changes. We
18 felt we professionals might ultimately understand it.
19 I don't know if anybody else would.

20 MR. STEVENSON: I don't have anything more to
21 add.

22 MR. LOOMIS: I wonder if I could follow up on
23 one point that Mr. Stevenson made, to see if I understood
24 him correctly.

25 Mr. Stevenson, I understand, indicated that

1 Immure securities would have an interest in maintaining a
2 market in the Sony rights for the benefit of the American
3 stockholders, and suggested if I got it correctly, that other
4 Japanese securities dealers might have a similar interest
5 in maintaining a similar market, for rights, which might
6 be acquired by investors holding A.D.R.'s of other Japanese
7 issuers.

8 I wonder what the nature of that interest was, and
9 how it would manifest itself?

10 MR. STEVENSON: Well, I think I said that I
11 was not competent to speak but that I assumed that if they
12 are interested in promoting a favorable market in the
13 United States for Japanese securities that certainly the
14 rights problem must be handled so therefore, it would seem
15 to me that it would be in every one's interest to have
16 the rights handled in a fair, decent way.

17 I was just addressing myself to the motivation.

18 I had just one other point on it.

19 In the case of Sony of course, the rights were also
20 registered. The rights offering was registered so a
21 considerable number of stockholders exercised their rights
22 rather than selling them.

23 MR. LOONIS: I wonder if Mr. Froy has anything?

24 MR. FROY: May I say, the expression "favorable"
25 is naturally a very relative expression. If it is favorable

1 for the owner of the rights or for the purchaser of those
2 rights, you see, and this is very difficult to determine,
3 and you have no means of using an open or free market.

4 MR. STEVENSON: Well, I don't think anyone would
5 deny that there is a problem because by nature, as far as
6 Japanese securities are concerned, exercise of rights is the
7 normal pattern.

8 MR. LOOMIS: The trouble I have with the whole
9 situation is the assumption on which you made your
10 statement.

11 MR. COMEN: That "if" of yours is a very large
12 "if". That "if", as I understand it, is that if a Japanese
13 firm would be interested in maintaining an orderly market
14 for the rights, I was led to believe that there is earlier
15 discussions, and discussion this morning, normally there
16 is not much of a market for rights and that would mean the
17 Japanese dealer who might have no interest whatsoever in the
18 A.D.R.'s arrangement here, or its successor, active
19 successor might have some interest themselves, in creating
20 a market where none exists. That is the "if", and that
21 is a fairly large "if", as I see it.

22 MR. STEVENSON: All I am saying is that if this
23 does not happen and that if investors do suffer very
24 severely as a result of this, it will reflect unfavorably
25 on the Japanese security business in general; so I would

1 assume that there, the H.A.S.D., which I understand does
2 exist, would have the same sort of interest that Mr. Froy
3 does here in seeing that people get a fair deal.

4 That is all I am addressing myself to.

5 MR. LOOMIS: There is one other aspect to this,
6 I wanted to go into just a little.

7 As I understood what was stated earlier, there
8 is no provision for the transfer of rights by Japanese
9 residents, and thus, the rights which are acquired by them
10 are all exercised?

11 MR. STEVENSON: Or lapse.

12 MR. LOOMIS: But I don't see why anybody in his
13 right mind would let that happen.

14 MR. STEVENSON: Right. It does happen.

15 MR. LOOMIS: Accordingly, the only transferable
16 rights are those held by foreign stockholders?

17 MR. STEVENSON: Right.

18 MR. LOOMIS: As I understand what was said earlier,
19 about 95 percent of the foreign stockholders have been
20 estimated to be Americans -- maybe it is 90 percent. Under
21 the Securities Act, unless the Sony procedure was followed,
22 it would be difficult for them to exercise rights, and it
23 sounds like a sort of a one way market to me, with only
24 sellers around, and that is the trouble.

25 MR. COHEN: That is part of the "if".

1 MR. STEVENSON: I think there is one point, as
2 I understand it. There is an active one-issue market in
3 Japan. You can of course, estimate what a fair price
4 for your rights would be by seeing what the subscription
5 price is and the present market price is. Obviously, if
6 the differential is too great you have a cause for complaint.

7 MR. COHEN: At the very least, I would assume from
8 what you said, Mr. Stevenson, that assuming there was enough
9 interest generated among Japanese dealers, to acquire
10 the securities at such a discount of the market value
11 of the shares, that the competition might create a market
12 for these rights in Japan; that is what would flow from
13 the situation if it developed as you suggested but there
14 would be an upper limit on that which would be the amount
15 of discount or the smallest amount of discount which
16 would attract Japanese dealers into this picture on
17 top of which, would have to be added the cost of transporta-
18 tion and insurance and so on.

19 MR. STEVENSON: Sure.

20 MR. BROWNELL: That is right.

21 MR. COHEN: Does anybody else want to speak on
22 this problem?

23 I can only say, by way of an aside, I once
24 spent a day sitting at the side of an arbitrageur
25 in London. It was a magnificent experience.

1 MR. FROY: Trading is easier there.

2 MR. COHEN: Easier than in Japan or the United
3 States?

4 MR. FROY: In Japan it is very easy because in a
5 way, you can make your own markets in some cases.

6 MR. COHEN: All jesting aside, does anybody else
7 want to add to this discussion or this point?

8 I take it that we have in some measure, encompassed
9 a number of disclosure problems in discussing the general
10 situation in Japan. Perhaps we ought to address ourselves
11 to the problem of duplication.

12 By that, I mean the issuance of A.D.R.'s by more
13 than one bank for the same security.

14 It may be the fairest way of dealing with this
15 is to first provide an opportunity to the opponents to
16 state the case.

17 Who wants to undertake that?

18 MR. CARR: May I say something first?

19 This is a matter of great interest to banks.
20 It is a matter which proliferates ideas; makes us verbose.
21 Should we start now and go on for 25 minutes or would it
22 not be more logical to do it all at once, at one hearing?

23 MR. COHEN: It is all right with me, whichever
24 way you gentlemen choose. I know your time is limited.

1 MR. BROWNELL: I think the opponents have come a
2 long ways. I would like to hear what the opponents --
3 who have the burden of proof -- have to say on that before
4 we break up.

5 MR. COHEN: May be we can do that. Maybe Mr.
6 Austin can make a statement, and we will adjourn when
7 he completes his statement. You can also add to it.
8 Then we can have another meeting, when we will really
9 square off.

10 MR. AUSTIN: Mr. Cohen, this duplication which
11 we are all familiar with, here we have the situation which
12 I think Mr. Brownell quite aptly terms "two men on a horse".
13 That is a condition which makes the horse difficult to
14 control and very uncomfortable for the rider, but it is
15 also, I think, a hazard to traffic -- in this case, the
16 public interest -- in the form of an orderly market.

17 The situation arises solely from a duplication
18 by Guarantee Trust Company of not less than 18 A.D.R.
19 issues first offered by other banks, not including four
20 Japanese issues now on file with the Commission.

21 The argument that such course is a beneficial
22 one to the public overlooks I think, a few aspects which
23 must be considered.

24 Clearly, all A.D.R.'s should not be duplicated,
25 only ones selected for their prominence and profitability.

1 Second, where does it end? I mean, if it is
2 argued that duplication is good, what is it duplication of?
3 What duplicate, which certainly is open to any bank at the
4 present time if anybody wants to go in them. What happens
5 when an issue is duplicated?

6 There are real pitfalls having to do with the
7 recordation as well as the rate in dollars to be paid.

8 There are others of a nature which I can
9 support in the record, where for example, a distribution
10 must be made under an estate; the decedent has in his
11 estate, A.D.R.'s of different kinds, with the same under-
12 lying security and the distribution cannot be made because
13 they cannot make a proper allocation among the heirs
14 and in all of these cases, the confusion would be worse
15 confounded in these cases where the duplicatee did not
16 conform to the request of the duplicator, to make uniform
17 records; dates of dividends. Aside from any question of
18 ethics, which I will not go into; some of us think it
19 is involved here -- we have the further projection of
20 this thing to a point where, for example, as a result
21 of a spread in the over-the-counter market, some one of
22 these companies might want a listing.

23 It has happened in the case of Transport
24 Trading; in the case of Markatina, and I am sure that the
25 stock exchange would never consider listing two A.D.R. issues

for the same underlying shares. Its reasons not to do so would be that it would be impossible to have an orderly market with two duplicate issues under the same name.

I would be glad to hear from others who think along the same lines as that.

MR. COHEN: You did not take a great deal of time. Mr. Carr, do you care to answer that?

MR. CARR: Well, I agree with what Mr. Austin says. It is only because of the efforts of those who have suffered a duplication that we are able to keep this market orderly at all. If there is a different record date for any purpose, if there is a different payment date for dividends, you can imagine the confusion of a man who is holding a Morgan Guarantee A.D.R. and an Irving A.D.R. He gets two checks on two different dates for the same security. If we don't happen to use the same factor for translating pounds or Dutch marks into dollars, he gets a different payment of dividend per share. All this is very confusing.

Supposing a man has one Morgan Guarantee and one Chemical Bank offering in the same stock? There is a stock dividend. He may get, instead of a full share which he would have gotten had he had all in one particular place, he may get two fractions. Instead of getting his share, he gets cash, which he does not want. He wants to keep his investment in this stock. I am sure that the

1 dealer fraternity has a great deal to say on the confusion
2 that arises in their back offices because of the duplication
3 of the A.D.R.'s.

4 Now, I will be glad to hear from other banks
5 or from NASD.

6 MR. DOYLE: The First National City Bank, as a
7 matter of principle, is against duplication. We find ourselves
8 in the position of not being duplicated, nor duplicating.

9 MR. CARR: I might now call on the Manufacturers
10 Trust.

11 MR. TRAVERS: We have not taken any position. We know
12 they exist. We, I suppose, are assuming certain things,
13 having taken place in the past they may take place with us
14 if and when we get into this.

15 MR. AUSTIN: Do you mean you will be duplicated,
16 or duplicating?

17 MR. TRAVERS: Duplicating.

18 MR. COHEN: I suppose you all don't believe in
19 the old adage about what is the highest form of flattery.

20 MR. FROY: Well, I have made a few notes.

21 Allow me to read those to you.

22 Coming to a point which many people call,
23 erroneously, controversial, I believe that if one person
24 is in favor and twelve persons are in a position of accord,
25 this cannot really be called controversial.

1 My Committee and I particularly hold a very
2 strong view on this point; strong views, not from the
3 trader's point of view, who is not interested in what he
4 trades as long as there is a margin of profit; from the
5 view of the public ad hoc, and also the dealer-brokers
6 and NASD point of view. The fact that several banks
7 are issuing A.D.R.'s for the same corporation, has given
8 a lot of trouble to the public who are the ultimate losers.

9 Also, to the offices in double work, and there is no
10 reason why this should not become ultimately a triple
11 or a quadruple duplication, if you like, but also, the
12 partners of those firms who had to make up losses because
13 of dividend payment, right proceedings, losses on
14 account of transactions, and complications resulting
15 from different book closing dates is a very serious point
16 which the trader generally does not see in the course of
17 his activity.

18 In the case of European A.D.R.'s this has
19 been a great nuisance. I can even quote examples.
20 I don't want to do it now, because I have some letters
21 here which will take a terrific controversial discussion.

22 This problem might become insurmountable
23 in the case of the Japanese A.D.R.'s where right
24 issues are the rule rather than the exception; where
25

no official study of exchange market exists for such rights, and where the differences between the different A.D.R. banks may be considerable.

It is difficult to think that the banks who are acting -- and I must repeat myself, as cloakroom attendants, for which a very handsome service fee is paid, by the trading community -- should foster facilities over and above those which we do require.

I am aware that letters can be produced here, obtained from traders, stating that duplication is desirable based on a slogan, competition is good for business, with which I agree except that the beneficiary of the competition should be the public at large. It should, possibly, profit from a reduction of A.D.R. fees but no such benefit has so far come to the public, in spite of the fact that some banks have issued their first A.D.R.'s in 1925 -- my secretary typed 1825. Maybe the period to show the advantage of this competition has not been long enough. To put a final proof to this argument, I can only repeat that my Committee, with one exception, voted against such duplication and that the Chairman of the Cashiers Division of the Association of Stock Exchange Firms, confirms at random inquires that its members feel the same way as my Committee does. They are the ultimate sufferers. They have the duplication to keep in their

1 books. They have to fight it out in their Dividend Department,
2 and they have to charge our accounts, ultimately, for the
3 losses.

4 If all this is not sufficient proof for my
5 argument, may I add that neither the New York Stock Exchange
6 nor the American Stock Exchange has ever given permission
7 that two different banks can act as issuing houses for any
8 of the A.D.R.'s quoted on those two exchanges. Their
9 experience in maintaining an orderly market should become
10 sort of a glowing example for the NASD to imitate, and
11 the Securities and Exchange Commission could take due note
12 that the maintenance of an orderly market is the best
13 protection for the public and makes it possible to increase
14 the influence of our market on an international level,
15 world wide.

16 I am not trying to make a speech but I want
17 you to know that this feeling is based on the desire
18 to see the public well protected, if the broker-dealer
19 is furnished with an instrument which he can easily handle
20 and banks receive an income which they should enjoy
21 for the service they are rendering.

22 That is all I have to say about duplication,
23 because most of the details have already been mentioned
24 by Mr. Austin and Mr. Carr.
25

1 MR. COHEN: May I just ask one question. I will
2 ask Mr. Brownell to say a few words, if he will, so that
3 your colleagues may take away some thoughts to consider.

4 Has the NASD considered whether it has any
5 authority to deal with this problem, insofar as its members
6 may trade in A.D.R.'s?

7 MR. FROY: We have discussed it with our
8 Executive Director and I believe with Mr. Grecco. We
9 have not found mention of regulating it on our level.

10 MR. COHEN: Now, I will not speak to it further,
11 but by doing that, I don't want to be understood that I
12 necessarily agree with that conclusion.

13 MR. BROWNELL: You want this to be brief, and
14 not complete.

15 MR. COHEN: These gentlemen want to make a 4:00
16 o'clock plane.

17 MR. BROWNELL: I won't use any more time than
18 they used. Maybe when we meet again, we can discuss
19 it further.

20 Mr. Cohen, I am really surprised to find four
21 banks and the NASD taking a position of this kind before
22 the staff of this Commission because I thought that we
23 all accepted the principle of competition between
24 banks. I don't think that there is any more confusion
25 involved in different banks issuing A.D.R.'s than there is

1 in different banks charging different interest rates or
2 custody rates or things of that kind.

3 I must point again to the fact that Morgan
4 Guarantee has been in this business perhaps as long --
5 and I think longer than any of these other banks and has
6 built up a reputation over the years and does have a
7 great many A.D.R. issues outstanding.

8 I am not in a position to put on outside witnesses
9 to prove it but I think their service has been so good as
10 to give them a strong competitive position and they are
11 willing to take on all competitors.

12 I am sure that the other banks must be equally
13 willing to take on all competitors and that their reasons
14 stem from the point that they have made about confusion
15 existing in the market itself.

16 However, I doubt that confusion.

17 I knew that we would be outnumbered at this
18 hearing today and our people therefore, took pains to
19 consult other brokers and dealers in the street and
20 asked them about the extent of the confusion that
21 arose.

22 I will submit to the Commission -- and of course,
23 copies to my friends here -- a letter addressed to the
24 Securities and Exchange Commission, marked to your
25 attention, dated June 13, 1961 and reads as follows:

"Dear Sir:

"The purpose of this letter is to inform the Securities and Exchange Commission that we, the undersigned, do not agree that the statement of opinion of the Chairman of the Foreign Securities Committee or the National Association of Securities Dealers, Inc., that duplication of A.D.R. facilities for the same foreign country by more than one depositor results in a disorderly market.

We realize that duplication has existed since 1955 involving some sixteen companies, and we fully appreciate that duplication is not the ideal solution of the problem.

We nevertheless urge that the Securities and Exchange Commission permit the continuance of the policy of the Morgan Guaranty and Trust Company of New York in duplicating any A.D.R. facilities, whenever demand warrants such duplication."

That is signed by some 25 or 26 firms, all, I am sure, well known to the Commission. I won't attempt to read the list.

MR. FROY: Are these signed by partners of that firm?

1 MR. BROWNELL: Mr. Moxley informed me that the
2 signatures are either by officers in the case of corporations,
3 or partners in the case of partnerships, or in some cases, by
4 arbitrageur in the case of an arbitrage firm.

5 He also says to me that he would appreciate it if
6 the names of these firms were not disclosed at this time,
7 and I have introduced -- I have given you the letter.
8 I will give you the letter of course, with names on it,
9 and I don't have to give the letter since I have read it.
10 Maybe we can discuss that question again.

11 MR. CARR: It hardly seems right to give weight
12 to evidence which is withheld from other parties if there
13 is a dispute.

14 MR. BROWNELL: I would like to withhold it
15 and discuss it with you. If the Commission wants it, it
16 is all right with me. Mr. Moxley spoke to me at this moment
17 about it. I don't think we will have difficulty in coming
18 to a proper agreement on it. I have no question as to the
19 validity of these signatures, and at the proper time, we
20 will give you any evidence you want with respect to the
21 execution.

22 MR. COHEN: I think Mr. Frey wanted to say
23 something on that.

24 MR. FROY: Mr. Cohen, I did not want to bring up
25 anything unpleasant at this meeting, because I felt this

1 was a meeting where we are trying to explore the possibilities
2 to protect the public, but this letter was known to me, of
3 which the street has spoken to me for the last ten days. It
4 has one very strange signature. I want you to know about it.

5 One firm which has a representative on our Committee
6 who voted strongly against duplication, was contacted, but
7 the man who was actually the member of our Committee knew
8 nothing about this letter until I told him about it.

9 I don't think that is a fair way of soliciting
10 a fair opinion on a matter which has been decided by
11 a representative body of firms who are represented on that
12 Committee, which I have the honor to serve as Chairman of.

13 MR. BROWNELL: Mr. Froy's point only proves we
14 frequently find differences of opinion between partners,
15 and the fact that one partner did not agree with the
16 other does not bother me in the slightest. I don't know
17 who the firm is or who the man is.

18 There is the letter. Let it speak for itself,
19 and of course, any member of this group who wants to
20 question the reliability of the execution, I will make
21 it possible to do it.

22 MR. COHEN: May I say this.

23 MR. CARR: If we should be allowed to know the
24 names of the secret witnesses, maybe we can get letters
25 from the same firm, expressing a different opinion.

1 MR. BROWNELL: Maybe they could.

2 I don't want to emphasize the letter any
3 further. It speaks for itself, and I will give it to you.

4 Let me -- because my self-allotted time is running
5 out, unless you want to talk about the letter further --
6 speak to my next point.

7 None of these gentlemen who opposed duplication
8 suggested any way in which it can be legally avoided.
9 There are different possible ways, I suppose, that all
10 of the banks could get together and make an agreement,
11 dividing up the business among themselves. We take the
12 first three letters of the alphabet.

13 You can take the first, the second, and the
14 third letters of the alphabet all the way down, all the
15 way around the world. Among this group of lawyers,
16 I don't need to do more than suggest that anything that
17 involves interstate commerce, whether it be securities in
18 the foreign country that are sold in interstate commerce,
19 I am sure none of the lawyers would allow their companies
20 to get involved in that matter.

21 The second possible way that occurs to me
22 would be to have the Securities and Exchange Commission
23 relied on in the field. I can visualize a hearing. It
24 will take some weeks but we all would prove our little case;
25 we would all ask for this and for that; then the Commission

1 which has decided more difficult problems, might if it
2 wishes, come down and divide up the field. I feel
3 reasonably sure you will not take that on in addition
4 to your other duties.

5 The third way that occurs to me is that the rule
6 of first come, first serve, would apply. In other words,
7 we would have a race of diligence. If any bank got its
8 hands on a particular issue first, it would have
9 that issue.

10 If the filing of the S-12 does not involve
11 necessary cooperation of the company, any energetic bank
12 from Mississippi could go out and file S-12's for two or
13 three hundred companies. They would be first in. No one
14 else would be able to take them away from them.

15 There may be other ways of doing it. I think
16 they are all variations of those three, all of which I
17 think are impossible and I submit that the well established
18 rule of fair competition in a field of this kind, is in
19 the interests of the public.

20 I will, when we meet again on it, talk to
21 you further about the much exaggerated complications
22 that result from the duplication but that is too long
23 a subject to go into now, except to say as these
24 gentlemen have said, no serious complication has so far
25 resulted.

1 MR. COHEN: Before we conclude, I neglected
2 this morning to identify for the record all of the people
3 who are in this room and although this may be repetitious,
4 we will start at the end of the table and go around
5 the room. Will you identify yourself?

6 MR. AUSTIN: Everybody here has presented an
7 appearance.

8 MR. COHEN: How about the second table?

9 MR. DOYLE: Everybody here identified themselves.

10 MR. COHEN: How about you gentlemen in the back?

11 MR. BATOR: My name is Bator. B-A-T-O-R. I am
12 an associate of Mr. Brownell.

13 I have not spoken.

14 MR. STEINER: Henry Steiner of Sullivan and
15 Cronwell.

16 MR. COHEN: Are you here with Mr. Stevenson?

17 MR. STEINER: That is correct.

18 MR. MEDLOCK: Donald Medlock, with Winthrop,
19 Stinson, Putnam and Roberts.

20 MR. WOLFE: James R. Wolfe, of Simpson,
21 Thacher and Bartlett.

22 MR. COHEN: For whom are you appearing?

23 MR. WOLFE: Manufacturers Trust.

24 MR. DOYLE: Before you conclude, I would like
25 to point out the difference of our position from the others

1 in the event this proceeding should be determined
2 favorable in issuing the A.D.R.'s.

3 MR. COHEN: This is not a proceeding. This is
4 just a conference among us.

5 MR. DOYLE: That is a proper correction.

6 Our filings are not effective; we filed a
7 delaying amendment, so the five issues on which the City
8 Bank would like to become effective are a step behind
9 the others. That can be borne in mind, so we can proceed,
10 without an agreement of course.

11 MR. COHEN: I think in all fairness, if the
12 Commission determines there will be no further questioning,
13 and the others may go ahead, we will bear in mind you
14 should not be left behind.

15 MR. DOYLE: Thank you.

16 MR. FROY: May I hand you for your record the
17 letter from the Association of Stock Exchange from the
18 Cashiers Division, against the duplication of A.D.R.'s.

19 MR. COHEN: Thank you.

20 MR. BROWNELL: May I make a final statement for
21 the record. I spoke with Mr. Moxley. He says the letter
22 addressed to the Securities and Exchange Commission, we
23 will turn over to you, and Morgan Guarantee Trust Company
24 of New York have no objection to your giving it to any
25 of the banks or others here appearing, if you so desire.

1 I want to clear that up before we close.

2 MR. COHEN: Well, I take it Morgan Guarantees
3 has no objection to your reading the letter. It is a matter
4 of disclosure of the name?

5 MR. BROWNELL: We have no objection to your doing
6 it so long as you do it.

7 MR. COHEN: Well, you don't have enough copies
8 to go around today?

9 MR. BROWNELL: I am sorry. I have not.

10 MR. COHEN: You leave that with me. I will make
11 suitable arrangements if that seems to be the appropriate
12 thing to do.

13 MR. CARR: Thank you very much.

14 MR. COHEN: Thank you for coming, gentlemen,
15 and we will invite you down again.

16 (Whereupon, at 3:25 o'clock, p.m., the conference
17 was adjourned, sine die.)
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25

This is to certify that the attached proceedings before the
Securities and Exchange Commission in the matter of:

JAPANESE-AMERICAN DEPOSITORY

(Name of proceeding)

June 28, 1961-Washington, D.C.

(Place and date of hearing)

were had as therein appears, and that this is the original transcript
thereof for the files of the Commission.

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We have R/S for Jap securities.

Agree to reg. rights office.

Compare Sony R/S on exchange controls with recent R/S. Syn ASD Committee.

disclosure problems, 22, 90, 97,

Prepared to discuss 90
difficult to discuss 97, 100

exchange controls 59, 61, 04-67, 77-78, 97

3. Frequent rights offerings - dilution, 59, 61-67,

not easy to discuss of 70, 74, 75, 76-78,
difficult to discuss 96

4. Difficulties 110,

never a problem, 11

clearly market 110

different words in dates 112, 114

Other banks

criticism, 110-116

competition 116-118

7-

5. Promotes U.S. trading market,

3 & 2 not applicable to AD R/S - 8

Purpose to prevent introduction of lot of stocks -

not every stock, 9, 10, 17,

not ^{Procedures 22-38} necessary

policy to issue

AD R/S for stock not traded in US, 10, 18

Also concerned about introducing

securities about which info,

21, 41-46,

not generally available 11-13, 20, not done 17, 21

Should be info. available for brokers 18, 15

not ^{only} 23 act problems 13, 18, 19, 20,

Generated by banks - 23, 25, 2

know holdings in US - 23-4, 26, 27, 29, 30

Jap situation different 25-26

70% - not dependent on banks 40

Public should know risks 41-46, 79-80

Deal with

NASD resolution - Jap. regulations not acceptable, 47, 50

AJA's in advantage to underwriting 51

Eliminated back office problems 56

4. 5. 6. 7. 8. 9. 10. 11. 12. 13. 14. 15. 16. 17. 18. 19. 20. 21. 22. 23. 24. 25. 26. 27. 28. 29. 30. 31. 32. 33. 34. 35. 36. 37. 38. 39. 40. 41. 42. 43. 44. 45. 46. 47. 48. 49. 50. 51. 52. 53. 54. 55. 56. 57. 58. 59. 60. 61. 62. 63. 64. 65. 66. 67. 68. 69. 70. 71. 72. 73. 74. 75. 76. 77. 78. 79. 80. 81. 82. 83. 84. 85. 86. 87. 88. 89. 90. 91. 92. 93. 94. 95. 96. 97. 98. 99. 100.

Could not maintain orderly market - 84, 91

Small trading market now 95

impeding capital markets 94-99