parents, there may be potential danger in making the child's welfare, as determined by a state agency, the only consideration in deciding adoption issues.

Only where a court has already deprived a parent of custody or guardianship, his consent is and should not be required.[16] In the instant case, the father may well be regarded as having forfeited his rights.[17] Thus, the outcome of the principal case would probably have been the same had it arisen in Illinois or some other state requiring consent.[18]

SEC—Registration of Securities—Failure to Register Resulting in Penal Action against Broker Redistributing for Person Controlling Issuer—[Federal].—The respondent, a broker-dealer using the medium of the New York Stock Exchange, sold a substantial number of shares for a person controlling the issuer. Although the shares were registered under the Securities Exchange Act of 1934, there was no registration statement in effect under the Securities Act of 1933 as the issue had originally been distributed prior to the 1933 act. The SEC, proceeding under authority granted by the 1934 act[1] to penalize brokers who have wilfully violated the Securities Act of 1933, ruled that the respondent's transactions were not within the exemptions of the 1933 act, and that the respondent was therefore acting as an underwriter within the terms of the act and should have

[16] Ala. Code Ann. (Michie, 1940) tit. 27, § 3. Generally, the termination of parental rights should be decided in separate proceedings and should not become an issue in the adoption action. The conflict between such rights and the welfare of the child is a separate issue from the adoption itself. Many states provide for such termination in custody or guardianship proceedings in a juvenile court on recommendation of a social or administrative agency. Courts specializing in human relationships or domestic problems are more competent to deal with the various factors determining parental qualifications. Such determinations should be made only after a complete investigation by a worker trained in evaluating the importance of natural parents in relation to the welfare of the child.

[17] Even states requiring consent provide for the forfeiture of parental rights where the parent has abandoned, deserted or neglected the child. 4 Vernier, American Family Laws 346–93 (1936). In these situations parental rights have been terminated by the actions of the parent. Moreover if the parent has been imprisoned or adjudged insane, is a drug addict or habitual drunkard, his consent to the adoption is not required since he is deemed to be unfit to fulfill his obligations. Ibid.

[18] Baker v. Strahorn, 33 Ill. App. 59 (1889). The court allowed the grandparents to adopt their grandchild over the objection of the father. The mother had obtained a divorce on grounds of desertion and had been awarded custody. The court indicated that the welfare of the child is of prime importance, and caprice, obstinacy or opposition on the part of the nonconsenting parent should not be regarded. Ibid., at 60. Nims, The Illinois Adoption Law and Its Administration (1928). The Illinois rule is not changed in this respect by the new adoption statute. Ill. Ann. Stat. (Smith-Hurd, Supp. 1945) C. 4, § 4–1.

[1] Section 15 (b) of the Securities Exchange Act of 1934 empowers the Commission to revoke the registration of any broker who has wilfully violated any provision of the Securities Act of 1933. 48 Stat. 895 (1934), as amended, 15 U.S.C.A. § 780 (b) (1941). Section 15 A (l) (2) authorizes the Commission to suspend for a period not exceeding twelve months or to expel from a registered securities association any member thereof who has wilfully violated any provision of the Securities Act. 48 Stat. 881 (1934), as amended, 15 U.S.C.A. § 780–3 (l) (2) (1941).

registered the securities prior to their sale.[2] The respondent's membership in the National Association of Securities Dealers, Inc., was accordingly suspended for a period of twenty days. *In the Matter of Ira Haupt & Co.*[3]

The SEC's ruling, requiring registration of unsolicited brokers' transactions, represents a departure from previous administrative interpretations, and illustrates the Commission's view of the flexibility of the Securities Act of 1933 and its adaptability to changing market conditions. The general purpose of the act is to protect the investing public by promoting disclosure of information concerning securities publicly offered[4] through the mails or in interstate commerce. To this end the filing of registration statements and the use of prospectuses is made a prerequisite to the sale of all but certain exempted securities. Although shares originally distributed prior to the act are exempt from the registration requirements,[5] this exemption has been denied in the case of a resale to the public of a substantial number of shares held by persons controlling the issuer[6] on the ground that such a secondary distribution "may possess all the

[2] 48 Stat. 77 (1933), as amended, 15 U.S.C.A. § 77e (a) (1941).

[3] Securities Exchange Act of 1934, Release No. 3845 (1946).

[4] Although the terms "public offering" and "distribution" are not defined in the Securities Act, it has been said that they refer to every part of a pre-arranged program for the distribution of a substantial block of securities by means of which it finally reaches the investing public. In the matter of Oklahoma-Texas Trust, 2 S.E.C. 764 (1937), aff'd Oklahoma-Texas Trust v. Securities and Exchange Comm'n, 100 F. 2d 888 (C.C.A. 10th, 1939). While there are no fixed standards as to the amount of shares to be offered or of the number of offerees necessary to bring the transactions within the terms "public offering" of "distribution," certain criteria have been offered by the SEC's legal staff; one must consider all the circumstances surrounding the transactions including the number of offerees and their relationship to each other and the issuer, the number of blocks of shares offered, the size of the offering, and the manner of the offering. Opinion of General Counsel of Securities and Exchange Comm'n, Securities Act of 1933, Release No. 285 (1935). In the instant case, although the precise extent of the distribution could not be predetermined as it was conditioned upon the market price, the commission found, nevertheless, that a distribution within the meaning of the act had been made because it was clearly intended that a substantial block of shares would be sold.

[5] Section 3 (a) (1) of the Securities Act of 1933, 48 Stat. 75 (1933), as amended, 15 U.S.C.A. § 77c (a) (1) (1941), exempts "Any security which prior to . . . . the enactment of this title has been sold or disposed of by the issuer."

[6] ". . . . but this exemption shall not apply to any new offering of such security by an issuer or underwriter." Ibid. In referring to the definition of an "underwriter" in section 2 (11), the House report explains that "The last sentence of this definition defining 'issuer' to include . . . . persons controlling the issuer has two functions . . . . its second function is to bring within the provisions of the bill redistributions whether of outstanding issues or issues sold subsequently to the enactment of the bill. All the outstanding stock of a particular corporation may be owned by one individual or a select group of individuals. At some future date they may wish to dispose of their holdings and to make an offer of this stock to the public. Such a public offering may possess all the dangers attendant upon a new offering of securities. Wherever such a redistribution reaches significant proportions the distributor would be in the position of controlling the issuer and thus able to furnish the information demanded by the bill. This being so, the distributor is treated as equivalent to the original issuer and, if he seeks to dispose of the issue through a public offering, he becomes subject to the act. The concept of control herein involved is not a narrow one depending upon a mathematical formula of 51 per cent of voting power, but is broadly defined to permit the provisions of the act to become effective wherever the fact of control actually exists." H. Rep. 85, 73d Cong., 1st Sess. 13–14 (1933).

dangers attendant upon a new offering."[7] Since the respondent in the instant case sold shares in connection with a secondary distribution, his actions constitute him an underwriter within the meaning of the act[8] and subject to its registration requirements unless he is permitted to take advantage of the special exemption permitting unsolicited broker's transactions to be effected without prior registration.[9] It has been only comparatively recently that substantial distributions could be made without active solicitations by brokers connected with the distribution.[10] Before the development of the recent seller's market, members of the Commission's legal staff had suggested that active solicitations were necessary to deny the benefit of the special exemption even where the broker claiming the exemption was clearly an underwriter by reason of his connection with the distribution.[11] Indeed, six months before the instant ruling the SEC confirmed this conclusion by their ruling in *In the Matter of The United Corp.*[12] permitting that corporation to dispose of common stock of a subsidiary through brokers on the exchange without prior registration of the issue under the Securities Act. That situation was, however, distinguishable from the instant case since the entire transaction was effected under the supervision of the commission pursuant to Rule U-100 promulgated under the Public Utility Holding Company Act of 1935. Although there were solicitations present in the instant case, the commission did not base its determination upon that fact, but explicitly stated that the prior interpretations of the act were not controlling since they had been de-

[7] H. Rep. 85, 73d Cong. 1st Sess. 13-14 (1933).

[8] Section 2 (11) of the Securities Act of 1933 defines an underwriter as "any person who .... sells for an issuer in connection with, the distribution of any security..... As used in the paragraph the term 'issuer' shall include .... any person .... controlling the issuer....." 48 Stat. 74 (1933), as amended, 15 U.S.C.A. § 77b (11) (1941).

[9] 48 Stat. 77 (1933), as amended, 15 U.S.C.A. 77d (2) (1941).

[10] For an interesting commentary on public buying habits during the recent seller's market see Velie, Babes in Wall Street, 117 Collier's 12 (April 27, 1946).

[11] A former General Counsel for the Securities and Exchange Commission had stated that "It follows that even though the broker acting for the affiliated stockholder were to be held an underwriter, it would still be possible for his transactions to be entitled to the exemption afforded by Section 4(2) for unsolicited 'brokers transactions.' Implicit in this term would appear to be the requirement that the purported broker receive only his usual and customary commission, in connection with such sales, and that he effect such sales only by means customarily employed by a broker in the usual and regular execution of customers' orders. It would seem inevitable, as a practical matter, that where an affiliated stockholder is endeavoring to effect a disposition of all or a substantial part of his holdings, a broker or brokers executing transactions on his behalf would go beyond the function properly exercised in transactions with Section 4(2) and would therefore not be entitled to exemption under that Section." Throop and Lane, Some Problems of Exemption under the Securities Act of 1933, 4 Law & Contemp. Prob. 89 (1937). And see letter of former Security and Exchange Commissioner Edmunde Burke, Jr., Memorandum on Behalf of Respondents 43, In the Matter of Ira Haupt & Co., SEC Docket No. N.Y. 2284 (1946).

[12] Holding Company Act of 1935, Releases Nos. 6337 (1945), 6409 and 6649 (1946). It may be suggested that since the SEC's ruling granting the application was not in terms restricted to unsolicited brokers' transactions the commission has implied that even solicited purchases do not require registration.

veloped against the background of a buyer's market in which disposal of a substantial number of shares without some solicitation was improbable.[13] Although the securities involved were registered under the Securities Exchange Act, the additional protection afforded investors under the Securities Act of 1933 justifies the increased burden imposed upon brokers by this ruling.[14] This additional protection is of no avail, however, unless it is utilized by the investor. It has been said that a basic policy of the act is to protect investors by making available to them during the twenty day "cooling period" all the information necessary to an intelligent, informed evaluation of the worth of the securities *prior* to their purchase.[15] It would seem that this policy cannot be effectuated without modification of the act with respect to the prospectus. At present, sales of securities are permitted if "accompanied or preceeded by a prospectus,"[16] and the broker complies with the act by delivering copies of the prospectus to the exchange for re-delivery to purchasers upon the sale.[17] This practice closes an important avenue of reliable information until after the sale and makes the prospectus serve as a "rain check" rather than as an advisory instrument, i.e., inadequacy of the information contained in the prospectus may afford the purchaser a basis for recovery under the civil liabilities provisions of the Securities Act of 1933.[18] The commission had considered this problem when it was presented by a similar practice of dealers who market new securities over the counter—the taking of orders over the telephone as soon as the registration statement became effective and the delivering of prospectuses with the confirmation.[19] The commission's tentative solution, permitting the use of a sum-

[13] In the Matter of Ira Haupt & Co., Securities Exchange Act of 1934, Release No. 3485 (1946).

[14] Although the information contained in both acts is somewhat similar, the Securities Act affords additional protection to the investor because it contains more detailed disclosures relating to underwriters and promoters and its provisions pertaining to civil liabilities facilitate recovery by the investor. For comparisons of the acts see Hanna, The Securities Exchange Act as Supplementary of the Securities Act, 4 Law & Contemp. Prob. 256 (1937); Civil Liability for Misstatements in Documents Filed under Securities Act and Securities Exchange Act, 44 Yale L. J. 456 (1935).

[15] Address by James J. Caffrey, The Dissemination of Information under the Securities Act, Securities Act of 1933, Release No. 3165 (1946).

[16] 48 Stat. 77 (1933), as amended, 15 U.S.C.A. § 77e (b) (2) (1941).

[17] Rule 153, General Rules and Regulations under the Securities Act of 1933, as amended (1946).

[18] 48 Stat. 82 (1933), as amended, 15 U.S.C.A. § 77k (1941); 48 Stat. 84 (1933), 15 U.S.C.A. § 77l (1941).

[19] The commission hopes to encourage full use of the waiting period to disseminate information by providing that the use of a "red herring," prepared on the basis of the information contained in the registration statement as amended to correct the deficiencies pointed out in the commission's first letter of comment, will not be deemed an unlawful offer or solicitation of an offer. Further encouragement to the use of the "red herring" is afforded by the proposal that it be permitted to serve as a final lawful prospectus if the persons receiving it are sent short supplementary documents containing further information necessary to correct deficiencies of the registration statement as of its effective date. This would prevent the waste

mary and encouraging the use of the "red herring" prospectus, while suited to the relatively leisurely transactions effected over the counter, probably will not solve the problem as presented in the more active setting of the stock exchange. But the requirements of the act are not based solely on the belief that the investor will learn to protect himself. Information is brought to his attention by the newspaper publicity given to the rulings and releases of the commission concerning security issues,[20] and he benefits indirectly from the very existence of the prospectus and the widespread disclosure it brings about. Thus information which prior to the Securities Act was often undisclosed even to institutional buyers is now made available to investment counsel, the investment department of banks, and financial advisory services.

In view of the possibility of reliance upon the earlier interpretations of the act by brokers acting for a controlling person, it may be argued that the commission's application of the new interpretation to transactions which occurred before the interpretation was announced is tantamount to retroactive law making.[21] It is to be observed that not only are there possibilities of penal liabilities, as in the instant case, but that brokers are also subject to civil liabilities to pur-

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of material and effort under the present ruling which requires a final prospectus which duplicates most of the material found in the "red herring." The commission is rather hesitant concerning the use of a summary. If used at all, it will be used as a supplement to the "red herring" and not as a substitute for it. The summary, like the "red herring," will be required to reflect the change in the registration statement required by the commission's first letter of comment and it will be necessary to file copies with the commission a certain stated period of time before its use. Dissemination of Information in a Securities Act Registration Statement before the Effective Date, Securities Act of 1933, Release No. 3165 (1946). The SEC has announced the adoption of the proposal with respect to the use of the "red herring" in Rule 131 under the Securities Act of 1933. This rule will be effective for a trial period of six months. The use of the summary has been postponed for further consideration. Chicago Journal of Commerce, p. 1, col. 2 (Dec. 6, 1946).

[20] A release concerning an issue of securities of the Hayes Mfg. Corp. offers an excellent example of how the commission through the newspaper publicity afforded its releases protects the investor. Although the issuer had amended his registration statement to eliminate the deficiencies found by the commission, the commission, contrary to its customary practice, deemed it necessary to the public interest to release its comment upon the deficiencies. In the Matter of Hayes Mfg. Corp., Securities Act of 1933, Release No. 3151 (1946); Chicago Journal of Commerce, p. 7, col. 1 (Aug. 20, 1946); "How to Make $3,788,000 on $17,000; SEC Gets Details," Chicago Daily News, p. 26, col. 2 (Aug. 20, 1946). This practice assures public knowledge of the matter and tends to "chill the market." Underwriters hesitate to handle the security not only for fear that it will not sell but because of the undesirability of associating their names with a dubious venture.

[21] This administrative practice is probably unassailable, however, on the theory that the SEC is not changing the meaning of the statute but merely expressing what has always been the true meaning. Manhattan General Equipment Co. v. Comm'r, 297 U.S. 129 (1936). That the present interpretation coincides with the intent to separate exempt and non-exempt transactions on the distinction between the trading and the distribution of securities is supported by the comment of the House Committee on § 4(2), "Paragraph (2) exempts the ordinary brokerage transaction. Individuals may thus dispose of their securities according to the method which is now customary without any restrictions imposed either upon the individual or the broker. This exemption also assures an open market for securities at all times,

chasers under this ruling.[22] But since a redistribution such as that involved in the instant case may present all the dangers attendant upon a new offering of securities, the commission's ruling assures to the purchasing public at least the minimum protection which the Securities Act affords. To rule otherwise would not only deny to the general purchaser the benefits afforded by secondary sources of information and the protection of more rigorous provisions pertaining to civil liability afforded by the Securities Act of 1933, but would also deny the use of the prospectuses to that minority of prospective purchasers who may actually utilize them.

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even though a stop order against further distribution of such securities may have been entered. Purchasers, provided they are not dealers, may thus, in the event that a stop order has been entered, cut their losses immediately, if there are losses, by disposing of the securities. On the other hand, the entry of a stop order prevents any further distribution of the security." The meaning of § 4(2) is further illuminated by the House Committee's comment on § 2(12) which defines the term "dealer" to include brokers. "Transactions by a broker, however, provided they are true brokerage transactions, are not brought within the scope of the bill by the specific exemptions granted in paragraph (2) of section 4. The sole object of this definition is thus to subject brokers to the same advertising restrictions that are imposed upon dealers, so as to prevent the broker from being used as a cloak for the sale of securities." H. Rep. 85, 73d Cong., 1st Sess. 14, 16 (1933).

[22] 48 Stat. 82 (1933), as amended, 15 U.S.C.A. § 77k (1941); 48 Stat. 84 (1933), 15 U.S.C.A. § 77l (1941).