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Annotation

Validity, Construction, and Application of Securities Investor Protection Act of 1970 *(15 U.S.C.A. §§ 78aaa* et seq.)

23 A.L.R. Fed. 157

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ARTICLE:

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[*1c] Text of Securities Investor Protection Act

The full text of the Securities Investor Protection Act of 1970 *(15 U.S.C.A. §§ 78aaa–*78lll) is as follows:

§ 78aaa. Short title.—

This Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll],with the following table of contents [omitted herein], may be cited as the "Securities Investor Protection Act of 1970". (Dec. 30, 1970, P. L. 91–598 § 1(a), 84 Stat 1636.) n1

§ 78bbb. Application of Securities Exchange Act of 1934.—

Except as otherwise provided in this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll],the provisions of the Securities Exchange Act of 1934 *(15 U.S.C. sec. 78a* and fol.; hereinafter referred to as the "1934 Act") apply as if this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll] constituted an amendment to, and was included as a section of, such Act [*15 U.S.C.A. §§ 78a* et seq.]. (Dec. 30, 1970, P. L. 91–598 § 2, 84 Stat 1637.)

§ 78ccc. Securities Investor Protection Corporation—

(a) Creation.—There is hereby established a body corporate to be known as "Securities Investor Protection Corporation" (hereafter in this Act referred to as "SIPC"). SIPC shall be a nonprofit corporation and shall have succession until dissolved by act of the Congress. SIPC shall—

(1) not be an agency or establishment of the United States Government;

(2) be a membership corporation the members of which shall be—

(A) all persons registered as brokers or dealers under section 15(b) of the 1934 Act [*15 U.S.C.A. § 78o],* and

(B) all persons who are members of a national securities exchange, other than persons whose business as a broker or dealer consists exclusively of (i) the distribution of shares of registered open end investment companies or unit investment trusts, (ii) the sale of variable annuities, (iii) the business of insurance, or (iv) the business of rendering investment advisory services to one or more registered investment companies or insurance company separate accounts; and

(3) except as otherwise provided in this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], be subject to, and have all the powers conferred upon a nonprofit corporation by, the District of Columbia Nonprofit Corporation Act (DC Code, sec. 29–1001 and fol.).

(b) Powers.—In addition to the powers granted to SIPC elsewhere in this Act, SIPC shall have the power—

(1) to sue and be sued, complain and defend, in its corporate name and through its own counsel, in any court, State, or Federal;

(2) to adopt, alter, and use a corporate seal, which shall be judicially noticed;

(3) subject to the provisions of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], to adopt, amend, and repeal, by its Board of Directors, by laws and rules relating to the conduct of its business and the exercise of all other rights and powers granted to it by this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll];

(4) to conduct its business (including the carrying on of operations and the maintenance of offices) and to exercise all other rights and powers granted to it by this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]in any State or other jurisdiction without regard to any qualification, licensing, or other statute in such State or other jurisdiction;

(5) to lease, purchase, accept gifts or donations of or otherwise acquire, to own, hold, improve, use, or otherwise deal in or with, and to sell, convey, mortgage, pledge, lease, exchange or otherwise dispose of, any property, real, personal or mixed, or any interest therein, wherever situated;

(6) subject to the provisions of subsection (c), to elect or appoint such officers, attorneys, employees, and agents as may be required, to determine their qualifications, to define their duties, to fix their salaries, require bonds for them and fix the

penalty thereof;
(7) to enter into contracts, to execute instruments, to incur liabilities, and to do any and all other acts and things as may be necessary or incidental to the conduct of its business and the exercise of all other rights and powers granted to SIPC by this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]; and
(8) by bylaw, to establish its fiscal year.
(c) Board of Directors.—
(1) Functions.—SIPC shall have a Board of Directors which, subject to the provisions of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll],shall determine the policies which shall govern the operations of SIPC.
(2) Number and appointment.—The Board of Directors shall consist of seven persons as follows:
(A) One director shall be appointed by the Secretary of the Treasury from among the officers and employees of the Department of the Treasury.
(B) One director shall be appointed by the Federal Reserve Board from among the officers and employees of the Federal Reserve Board.
(C) Five directors shall be appointed by the President, by and with the advice and consent of the Senate, as follows—
(i) three such directors shall be selected from among persons who are associated with, and representative of different aspects of, the securities industry, not all of whom shall be from the same geographical area of the United States, and
(ii) two such directors shall be selected from the general public from among persons who are not associated with any broker or dealer, within the meaning of paragraph (18) of section 3(a) of the 1934 Act [*15 U.S.C.A. § 78c*(a)(18)], or similarly associated with a national securities exchange or other securities industry group and who have not had any such association during the two years preceding appointment.
(3) Chairman and vice chairman.—The President shall designate a Chairman and Vice Chairman from among those directors appointed under paragraph (2)(C)(ii) of this subsection.
(4) Terms.—
(A) Except as provided in subparagraphs (B) and (C), each director shall be appointed for a term of three years.
(B) Of the directors first appointed under paragraph (2)—
(i) two shall hold office for a term expiring on December 31, 1971,
(ii) two shall hold office for a term expiring on December 31, 1972, and
(iii) three shall hold office for a term expiring on December 31, 1973, as designated by the President at the time they take office. Such designation shall be made in a manner which will assure that no two persons appointed under the authority of the same clause of paragraph (2)(C) shall have terms which expire simultaneously.
(C) A vacancy in the Board shall be filled in the same manner as the original appointment was made. Any director appointed to fill a vacancy occurring prior to the expiration of the term for which his predecessor was appointed shall be appointed only for the remainder of such term. A director may serve after the expiration of his term until his successor has taken office.
(5) Compensation.—All matters relating to compensation of directors and the determination of dollar volume of trading on exchanges shall be as provided in the bylaws of SIPC.
(d) Meetings of Board.—The Board of Directors shall meet at the call of its Chairman, or as otherwise provided by the bylaws of SIPC.
(e) Bylaws.—
(1) As soon as practicable but not later than forty–five days after the date of enactment of this Act [Dec. 30, 1970], the Board of Directors shall adopt initial bylaws and rules relating to the conduct of the business of SIPC and the exercise of the rights and powers granted to it by this Act, and shall file a copy thereof with the Commission. Thereafter, the Board of Directors may alter, supplement, or repeal any existing bylaw or rule and may adopt additional bylaws and rules, and in each case shall file a copy thereof with the Commission.
(2) Each such initial bylaw or rule, alteration, supplement, or repeal, and additional bylaw or rule shall take effect upon the thirtieth day (or such later date as SIPC may designate) after the filing of the copy thereof with the Commission or upon such earlier date as the Commission may determine, unless the Commission shall, by notice to SIPC setting forth the reasons therefor, disapprove the same, in whole or in part, as being contrary to the public interest or contrary to the purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll],
(3) The Commission may, by such rules or regulations as it determines to be necessary or appropriate in the public interest or to effectuate the purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll],require the adoption, amendment, alteration of, supplement to or recession of any bylaw or rule by SIPC, whenever adopted.
(f) Other members.—
(1) Any person who is a broker, dealer, or member of a national securities exchange and who is excluded from membership

in SIPC under subsection (a) may become a member of SIPC under such conditions and upon such terms as SIPC shall require.

(2) Notwithstanding anything contained in subsections (c) and (d) of section 4, any person who becomes a member of the corporation under this subsection shall be subject to such assessments as SIPC determines to be equitable. (Dec. 30, 1970, P. L. 91–598 § 3, 84 Stat 1637.)

§ 78ddd. SIPC Fund.—

(a) In general.—

(1) Establishment of fund.—SIPC shall establish a "SIPC Fund" (hereinafter in this Act referred to as the "fund"). All amounts received by SIPC (other than amounts paid directly to any lender pursuant to any pledge securing a borrowing by SIPC) shall be deposited in the fund, and all expenditures made by SIPC shall be made out of the fund.

(2) Balance of the fund.—The balance of the fund at any time shall consist of the aggregate at such time of the following items:

(A) Cash on hand or on deposit.

(B) Amounts invested in United States Government or agency securities.

(C) Confirmed lines of credit.

(3) Confirmed lines of credit.—For purposes of this section, the amount of confirmed lines of credit as of any time is the aggregate amount which SIPC at such time has the right to borrow from banks and other financial institutions under confirmed lines of credit or other written agreements which provide that moneys so borrowed are to be repayable by SIPC not less than one year from the time of such borrowings (including, for purposes of determining when such moneys are repayable, all rights of extension, refunding, or renewal at the election of SIPC).

(b) Initial required balance for fund.—Within one hundred and twenty days from the date of enactment of this Act [Dec. 30, 1970], the balance of the fund shall aggregate not less than $75,000,000, less any amounts expended from the fund within that period.

(c) Assessments.—

(1) Initial assessments.—Each member of SIPC shall pay to SIPC, or the collection agent for SIPC specified in section 9(a) [*15 U.S.C.A. § 78iii]*, on or before the one hundred and twentieth day following the date of enactment of this Act [Dec. 30, 1970], an assessment equal to one–eighth of 1 per centum of the gross revenues from the securities business of such member during the calendar year 1969, or if the Commission shall determine that, for purposes of assessment pursuant to this paragraph, a lesser percentage of gross revenues from the securities business is appropriate for any class or classes of members (taking into account relevant factors, including but not limited to types of business done and nature of securities sold), such lesser percentages as the Commission, by rule or regulation, shall establish for such class or classes, but in no event less than one–sixteenth of 1 per centum for any such class. In no event shall any assessment upon a member pursuant to this paragraph be less than $150.

(2) General assessment authority.—SIPC shall, by bylaw or rule, impose upon its members such assessments as, after consultation with self–regulatory organizations, SIPC may deem necessary and appropriate to establish and maintain the fund and to repay any borrowings by SIPC. Any assessments so made shall be in conformity with the contractual obligations made by SIPC in connection with any borrowing incurred by SIPC. Subject to paragraph (3) and subsection (d)(1)(A), any such assessment upon the members, or any one or more classes thereof, may, in whole or in part, be based upon or measured by (A) the amount of their gross revenues from the securities business, or (B) all or any of the following factors: the amount or composition of their gross revenues from the securities business, the number or dollar volume of transactions effected by them, the number of customer accounts maintained by them or the amounts of cash and securities in such accounts, their net capital, the nature of their activities (whether in the securities business or otherwise) and the consequent risks, or other relevant factors.

(3) Limitations.—Notwithstanding any other provision of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll](other than section 3(f))—

(A) no assessment shall be made upon a member otherwise than pursuant to paragraph (1) or (2) of this subsection,

(B) an assessment may be made under paragraph (2) of this subsection at a rate in excess of one–half of one per centum during any twelve–month period if SIPC determines, in accordance with a bylaw or rule, that such rate of assessment during such period will not have a material adverse effect on the financial condition of its members or their customers, except that no assessments shall be made pursuant to such paragraph upon a member which require payments during any such period which exceed in the aggregate one per centum of such member's gross revenues from the securities business for such period, and

(C) no assessment shall include any charge based upon the member's activities (i) in the distribution of shares of registered open end investment companies or unit investment trusts, (ii) in the sale of variable annuities, (iii) in the business

of insurance, or (iv) in the business of rendering investment advisory services to one or more registered investment companies or insurance company separate accounts.

(d) Requirements respecting assessments and lines of credit.—

(1) Assessments.—

(A) 1/2 of 1 percent assessment.—Subject to subsection (c)(3), SIPC shall impose upon each of its members an assessment at a rate of not less than one-half of 1 per centum per annum of the gross revenues from the securities business of such member—

(i) until the balance of the fund aggregates not less than $150,000, 000 (or such other amount as the Commission may determine in the public interest),

(ii) during any period when there is outstanding borrowing by SIPC pursuant to subsection (f) or subsection (g) of this section, and

(iii) whenever the balance of the fund (exclusive of confirmed lines of credit) is below $100,000,000 (or such other amount as the Commission may determine in the public interest).

(B) 1/4 of 1 percent assessment.—During any period during which—

(i) the balance of the fund (exclusive of confirmed lines of credit) aggregates less than $150,000,000 (or such other amount as the Commission has determined under paragraph (2)(B)), or

(ii) SIPC is required under paragraph (2)(B) to phase out of the fund all confirmed lines of credit,

SIPC shall endeavor to make assessments in such a manner that the aggregate assessments payable by its members during such period shall not be less than one-fourth of 1 per centum per annum of the aggregate gross revenues from the securities business for such members during such period.

(2) Lines of credit.—

(A) $50,000,000 limit after 1973.—After December 31, 1973, confirmed lines of credit shall not constitute more than $50,000,000 of the balance of the fund.

(B) Phaseout requirement.—When the balance of the fund aggregates $150,000,000 (or such other amount as the Commission may determine in the public interest) SIPC shall phase out of the fund all confirmed lines of credit.

(e) Prior trusts.—Overpayments and underpayments.—

(1) Prior trusts.—There may be contributed and transferred at any time to SIPC any funds held by any trust established by a self-regulatory organization prior to January 1, 1970, and the amounts so contributed and transferred shall be applied, as may be determined by SIPC with approval of the Commission, as a reduction in the amounts payable pursuant to assessments made or to be made by SIPC upon members of self-regulatory organization pursuant to subsection (c)(2). No such reduction shall be made at any time when there is outstanding any borrowing by SIPC pursuant to subsection (g) of this section or any borrowings under confirmed lines of credit.

(2) Overpayments.—To the extent that any payment by a member exceeds the maximum rate permitted by subsection (c) of this section, the excess shall not be recoverable except against future payments by such member in accordance with a bylaw or rule of SIPC.

(3) Underpayments.—If a member fails to pay when due all or any part of an assessment made upon such member, the unpaid portion thereof shall bear interest at such rate as may be determined by SIPC bylaw or rule.

(f) Borrowing authority.—SIPC shall have the power to borrow moneys and to evidence such borrowed moneys by the issuance of bonds, notes, or other evidences of indebtedness, all upon such terms and conditions as the Board of Directors may determine in the case of a borrowing other than pursuant to subsection (g) of this section, or as may be prescribed by the Commission in the case of a borrowing pursuant to subsection (g). The interest payable on a borrowing pursuant to subsection (g) shall be equal to the interest payable on the related notes or other obligations issued by the Commission to the Secretary of the Treasury. To secure the payment of the principal of, and interest and premium, if any, on, all bonds, notes, or other evidences of indebtedness so issued, SIPC may make agreements with respect to the amount of future assessments to be made upon members and may pledge all or any part of the assets of SIPC and of the assessments made or to be made upon members. Any such pledge of future assessments shall (subject to any prior pledge) be valid and binding from the time that it is made, and the assessments so pledged and thereafter received by SIPC, or any examining authority as collection agent for SIPC, shall immediately be subject to the lien of such pledge without any physical delivery thereof or further act, and the lien of such pledge shall be valid and binding against all parties having claims of any kind against SIPC or such collection agent whether pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll], in tort, contract or otherwise, irrespective of whether such parties have notice thereof. During any period when a borrowing by SIPC pursuant to subsection (g) of this section is outstanding, no pledge of any assessment upon a member to secure any bonds, notes, or other evidences of indebtedness issued other than pursuant to subsection (g) of this section shall be effective as to the excess of the payments under the assessment on such member during any twelve-month period over

one–fourth of 1 per centum of such member's gross revenues from the securities business for such period. Neither the instrument by which a pledge is authorized or created, nor any statement or other document relative thereto, need be filed or recorded in any State or other jurisdiction. The Commission may by rule or regulation provide for the filing of any instrument by which a pledge or borrowing is authorized or created, but the failure to make or any defect in any such filing shall not affect the validity of such pledge or borrowing.

(g) SEC loans to SIPC.—In the event that the fund is or may reasonably appear to be insufficient for the purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], the Commission is authorized to make loans to SIPC. At the time of application for, and as a condition to, any such loan, SIPC shall file with the Commission a statement with respect to the anticipated use of the proceeds of the loan. If the Commission determines that such loan is necessary for the protection of customers of brokers or dealers and the maintenance of confidence in the United States securities markets and that SIPC has submitted a plan which provides as reasonable an assurance of prompt repayment as may be feasible under the circumstances, then the Commission shall so certify to the Secretary of the Treasury, and issue notes or other obligations to the Secretary of the Treasury pursuant to subsection (h). If the Commission determines that the amount or time for payment of the assessments pursuant to such plan would not satisfactorily provide for the repayment of such loan, it may, by rules and regulations, impose upon the purchasers of equity securities in transactions on national securities exchanges and in the over–the–counter markets a transaction fee in such amount as at any time or from time to time it may determine to be appropriate, but not exceeding one–fiftieth of 1 per centum of the purchase price of the securities. No such fee shall be imposed on a transaction (as defined by rules or regulations of the Commission) of less than $5,000. For the purposes of the next preceding sentence, (A) the fee shall be based upon the total dollar amount of each purchase; (B) the fee shall not apply to any purchase on a national securities exchange or in an over–the–counter market by or for the account of a broker or dealer registered under section 15(b) of the 1934 Act [*15 U.S.C.A. § 78o*(b)] or a member of a national securities exchange unless such purchase is for an investment account of such broker, dealer, or member (and for this purpose any transfer from a trading account to an investment account shall be deemed a purchase at fair market value); and (C) the Commission by rules and regulations may exempt any transaction in the over–the–counter markets in order to provide for the assessment of fees on purchasers in transactions in those markets on a basis comparable to the assessment of fees on purchasers in transactions on national securities exchanges. Such fee shall be collected by the broker or dealer effecting the transaction for or with the purchaser and shall be paid to SIPC in the same manner as assessments imposed pursuant to subsection (c).

(h) SEC Notes issued to treasury.—To enable the Commission to make loans under subsection (g), the Commission is authorized to issue to the Secretary of the Treasury notes or other obligations in an aggregate amount of not to exceed $1,000,000,000, in such forms and denominations, bearing such maturities, and subject to such terms and conditions, as may be prescribed by the Secretary of the Treasury. Such notes or other obligations shall bear interest at a rate determined by the Secretary of the Treasury, taking into consideration the current average market yield on outstanding marketable obligations of the United States of comparable maturities during the month preceding the issuance of the notes or other obligations. The Secretary of the Treasury may reduce the interest rate if he determines such reduction to be in the national interest. The Secretary of the Treasury is authorized and directed to purchase any notes and other obligations issued hereunder and for that purpose he is authorized to use as a public debt transaction the proceeds from the sale of any securities issued under the Second Liberty Bond Act, as amended [*31 U.S.C.A. §§ 752*–754b, 757b, 757c–757e, 758, 760, 764–766, 769, 771, 773, 774, 801], and the purposes for which securities may be issued under that Act, as amended, are extended to include any purchase of such notes and obligations. The Secretary of the Treasury may at any time sell any of the notes or other obligations acquired by him under this subsection. All redemptions, purchases, and sales by the Secretary of the Treasury of such notes or other obligations shall be treated as public debt transactions of the United States.

(i) Gross Revenues" defined.—

(1) In general.—For purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], the term "gross revenues from the securities business" means the sum of (but without duplication):

(A) commissions earned in connection with transactions in securities effected for customers as agent (net of commissions paid to other brokers and dealers in connection with such transactions) and markups in respect of purchases or sales of securities as principal,

(B) charges for executing or clearing transactions in securities for other brokers and dealers,

(C) the net realized gain, if any, from principal transactions in securities in trading accounts,

(D) the net profit, if any, from the management of or participation in the underwriting or distribution of securities,

(E) interest earned on customers' securities accounts,

(F) fees for investment advisory services (except when rendered to one or more registered investment companies or

insurance company separate accounts) or account supervision in respect of securities,
(G) fees for the solicitation of proxies with respect to, or tenders or exchanges of, securities,
(H) income from service charges or other surcharges in respect of securities,
(I) except as otherwise provided by rule or regulation of the Commission, dividends and interest received on securities in investment accounts of the broker or dealer,
(J) fees in connection with put, call, and other option transactions in securities, and
(K) fees and other income for all other investment banking services.
Such term does not include revenues received by a broker or dealer in connection with the distribution of shares of a registered open end investment company or unit investment trust or revenues derived by a broker or dealer from the sale of variable annuities or from the conduct of the business of insurance.
(2) Consolidated group.—Except as otherwise provided by SIPC by bylaw or rule, gross revenues from the securities business of a broker or dealer shall be computed on a consolidated basis for such broker or dealer and all its subsidiaries, and the operations of a broker or dealer shall include those of any business to which such broker or dealer has succeeded.
(3) Meaning of terms not defined.—SIPC may by bylaw or rule define all terms used in this subsection insofar as such definitions are not inconsistent with the provisions of this subsection. (Dec. 30, 1970, P. L. 91–598 § 4, 84 Stat 1639.)
§ 78eee. Protection of customers.—
(a) Determination of need of protection.—
(1) Notice to SIPC.—If the Commission or any self–regulatory organization is aware of facts which lead it to believe that any broker or dealer subject to its regulation is in or is approaching financial difficulty, it shall immediately notify SIPC, and, if such notification is by a self–regulatory organization, the Commission.
(2) Action by SIPC.—If SIPC determines that any member has failed or is in danger of failing to meet its obligations to customers and that there exists one or more of the conditions specified in subsection (b)(1)(A), SIPC, upon notice to such member, may apply to any court of competent jurisdiction specified in section 27 or 21(e) of the 1934 Act [*15 U.S.C.A. § 78aa* or 78u(e)] for a decree adjudicating that customers of such member are in need of the protection provided by this Act [*15 U.S.C.A. § 78aa* or 78u(e)].
(3) Effect of other pending actions.—An application under paragraph (2)—
(A) with the consent of the Commission, may be combined with any action brought by the Commission including an action by it for a temporary receiver pending an appointment of a trustee under subsection (b)(3), and
(B) may be filed notwithstanding the pendency in the same or any other court of any bankruptcy, mortgage foreclosure, or equity receivership proceeding or any proceeding to reorganize, conserve, or liquidate such member or its property, or any proceeding to enforce a lien against property of such member.
(b) Court action.—
(1) Issuance of decree.—
(A) Findings by court.—A court to which application is made pursuant to subsection (a)(2) shall grant the application and issue a decree adjudicating that customers of the member named in the application are in need of protection under this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll] if it finds that such member—
(i) is insolvent within the meaning of section 1(19) of the Bankruptcy Act [*11 U.S.C.A. § 1*(19)], or is unable to meet its obligations as they mature, or
(ii) has committed an act of bankruptcy within the meaning of section 3 of the Bankruptcy Act [*11 U.S.C.A. § 21],* or
(iii) is the subject of a proceeding pending in any court or before any agency of the United States or any State in which a receiver, trustee, or liquidator for such member has been appointed, or
(iv) is not in compliance with applicable requirements under the 1934 Act [*15 U.S.C.A. §§ 78a* et seq.] or rules or regulations of the Commission or any self–regulatory organization with respect to financial responsibility or hypothecation of customers' securities, or
(v) is unable to make such computations as may be necessary to establish compliance with such financial responsibility or hypothecation rules or regulations.
(B) Uncontested applications.—If within three business days after the filing of an application pursuant to subsection (a)(2), or such other period as the court may order, the debtor shall consent to or fail to contest such application or shall fail to show facts sufficient to controvert any material allegation of such application, the court shall forthwith grant the application and issue a decree adjudicating that customers of the member named in the application are in need of protection under this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll].
(2) Exclusive jurisdiction over debtor.—Upon the filing of an application pursuant to subsection (a)(2), the court to which application is made shall have exclusive jurisdiction of the debtor involved and its property wherever located with the powers, to the extent consistent with the purposes, of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], of a court

of bankruptcy and of a court in a proceeding under chapter X of the Bankruptcy Act [*11 U.S.C.A. §§ 501* et seq.] . Pending an adjudication under paragraph (1) such court shall stay, and upon appointment by it of a trustee as provided in paragraph (3) such court shall continue the stay of, any pending bankruptcy, mortgage foreclosure, equity receivership, or other proceeding to reorganize, conserve, or liquidate the debtor or its property and any other suit against any receiver, conservator, or trustee of the debtor or its property. Pending such adjudication and upon the appointment by it of such trustee, the court may stay any proceeding to enforce a lien against property of the debtor or any other suit against the debtor. Pending such adjudication, such court may appoint a temporary receiver.

(3) Appointment of trustee.—If the court grants an application and makes an adjudication under paragraph (1), the court shall forthwith appoint as trustee for the liquidation of the business of the debtor in accordance with section 6 [*15 U.S.C.A. § 78fff],* and as attorney for such trustee, such persons as SIPC shall specify. No person shall be appointed as such trustee or attorney if such person is not "disinterested" within the meaning of section 158 of the Bankruptcy Act [*11 U.S.C.A. § 588]*.

(4) Debtor and filing date defined.—For purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]—

(A) Debtor.—The term "debtor" means a member of SIPC in respect of whom an application has been filed pursuant to subsection (a)(2).

(B) Filing date.—The term "filing date" means the date on which an application with respect to any debtor is filed under subsection (a)(2); except that if—

(i) a petition was filed before such date by or against the debtor under the Bankruptcy Act [*11 U.S.C.A. §§ 1* et seq.], or

(ii) the debtor is the subject of a proceeding pending in any court or before any agency of the United States in which a receiver, trustee, or liquidator for such debtor was appointed which proceeding was commenced before the date on which such application was filed,

then the term "filing date" means the date on which such petition was filed or such proceeding commenced.

(c) SEC participation in proceedings.—The Commission may, on its own motion, file notice of its appearance in any proceeding under this Act and may thereafter participate as a party. (Dec. 30, 1970, P. L. 91–598 § 5, 84 Stat 1644.)

§ 78fff. Liquidation proceedings.—

(a) General purposes of liquidation proceedings.—The purposes of any proceeding in which a trustee has been appointed under section 5(b)(3) [*15 U.S.C.A. § 78eee*(b)(3)] (hereinafter in this section referred to as a "liquidation proceeding") shall be:

(1) as promptly as possible after such appointment and in accordance with the provisions of this section—

(A) to return specifically identifiable property to the customers of the debtor entitled thereto;

(B) to distribute the single and separate fund, and (in advance thereof or concurrently therewith) pay to customers moneys advanced by SIPC, as provided in subsection (f);

(2) to operate the business of the debtor in order to complete open contractual commitments of the debtor pursuant to subsection (d);

(3) to enforce rights of subrogation as provided in this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], and

(4) to liquidate the business of the debtor.

(b) Powers and duties of trustee.—

(1) Trustee powers.—A trustee appointed under section 5(b)(3) [*15 U.S.C.A. § 78eee*(b)(3)] (hereinafter referred to as "trustee") shall be vested with the same powers and title with respect to the debtor and the property of the debtor, and the same rights to avoid preferences, as a trustee in bankruptcy and a trustee under chapter X of the Bankruptcy Act [*11 U.S.C.A. §§ 501* et seq.] have with respect to a bankrupt and a chapter X debtor. In addition, a trustee shall have the right—

(A) with the approval of SIPC, to hire and fix the compensation of all personnel (including officers and employees of the debtor and of its examining authority) and other persons (including but not limited to accountants) that are deemed by such trustee necessary for all or any purposes of the liquidation proceeding, and

(B) to operate the business of the debtor in order to complete open contractual commitments pursuant to subsection (d),

and no approval of the court shall be required therefor.

(2) Trustee duties.—Except as inconsistent with the provisions of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]or otherwise ordered by the court, a trustee shall be subject to the same duties as a trustee appointed under section 44 of the Bankruptcy Act [*11 U.S.C.A. § 72],* except that a trustee may, but shall have no duty to, reduce to money any securities in the single and separate fund (provided under subsection (c)(2)(B)) or in the general estate of the debtor.

(c) Application of Bankruptcy Act.—

(1) General provisions applicable.—Except as inconsistent with the provisions of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll] and except that in no event shall a plan of reorganization be formulated, a liquidation proceeding shall be conducted in accordance with, and as though it were being conducted under, the provisions of chapter X [*11 U.S.C.A. §§*

501 et seq.] and such of the provisions (other than section 60e [*11 U.S.C.A. § 96*(e)]) of chapters I to VII [*11 U.S.C.A. §§ 1*–112], inclusive, of the Bankruptcy Act as section 102 of chapter X [*11 U.S.C.A. § 502]* would make applicable if an order of the court had been entered directing that bankruptcy be proceeded with pursuant to the provisions of such chapters I to VII, inclusive; except that the court may, for such period as may be appropriate, stay enforcement of, but shall not abrogate, the rights provided in section 68 of the Bankruptcy Act [*11 U.S.C.A. § 108]* and the right to enforce a valid, non–preferential lien or pledge against the property of the debtor. For purposes of applying the Bankruptcy Act [*11 U.S.C.A. §§ 1* et seq.] in carrying out this section, any reference in the Bankruptcy Act to the date of commencement of proceedings under the Bankruptcy Act shall be deemed to be a reference to the filing date (as defined in section 5(b)(4)(B)).

(2) Special provisions.—The following subparagraphs of this paragraph shall apply to a liquidation proceeding in lieu of section 60e of the Bankruptcy Act [*11 U.S.C.A. § 96*(e)]:

(A) Definitions.—Except as otherwise expressly provided in this section, for purposes of this section and the application of the Bankruptcy Act [*11 U.S.C.A. §§ 1* et seq.] to a liquidation proceeding—

(i) property" includes cash and securities, whether or not negotiable and all property of a similar character;

(ii) customers" of a debtor means persons (including persons with whom the debtor deals as principal or agent) who have claims on account of securities received, acquired, or held by the debtor from or for the account of such persons (I) for safekeeping, or (II) with a view to sale, or (III) to cover consummated sales, or (IV) pursuant to purchases, or (V) as collateral security, or (VI) by way of loans of securities by such persons to the debtor, and shall include persons who have claims against the debtor arising out of sales or conversions of such securities, and shall include any person who has deposited cash with the debtor for the purpose of purchasing securities, but shall not include any person to the extent that such person has a claim for property which by contract, agreement, or understanding, or by operation of law, is part of the capital of the debtor or is subordinated to the claims of creditors of the debtor;

(iii) cash customer" means, with respect to any securities or cash, customers entitled to immediate possession of such securities or cash without the payment of any sum to the debtor, and for purposes of this clause, the same person may be a cash customer with reference to certain securities or cash and not a cash customer with reference to other securities or cash;

(iv) net equity" of a customer's account or accounts means the dollar amount thereof determined by giving effect to open contractual commitments completed as provided in subsection (d), by excluding any specifically identifiable property reclaimable by the customer, and by subtracting the indebtedness, if any, of the customer to the debtor from the sum which would have been owing by the debtor to the customer had the debtor liquidated, by sale or purchase on the filing date, all other securities and contractual commitments of the customer, and for purposes of this definition, accounts held by a customer in separate capacities shall be deemed to be accounts of separate customers; and

(v) securities" has the same meaning as such term has under section 60e of the Bankruptcy Act [*11 U.S.C.A. § 96*(e)].

(B) Single and separate fund.—All property at any time received, acquired, or held by or for the account of a debtor from or for the account of customers except cash customers who are able to identify specifically their property in the manner prescribed in subparagraph (C), and the proceeds of all customers' property transferred by the debtor, including property unlawfully converted, shall constitute a single and separate fund; and all customers except such cash customers shall constitute a single and separate class of creditors, entitled to share ratably in such fund on the basis of their respective net equities as of the filing date and in priority to all other payments, except that (i) there shall be repaid to SIPC, in priority to all other claims payable from such single and separate fund, the amount of all advances made by SIPC to the trustee to permit the completion of open contractual commitments pursuant to subsection (d), and (ii) to the extent that any other assets of the debtor may be available therefor or as otherwise ordered by the court, all costs and expenses specified in clauses (1) and (2) of section 64a of the Bankruptcy Act [*11 U.S.C.A. § 104*(a)] shall be paid from such single and separate fund in priority to the claims of such single and separate class of creditors, and any moneys advanced by SIPC for such costs and expenses shall be recouped as such. If such single and separate fund shall not be sufficient to pay in full the claims of such single and separate class of creditors, the creditors of such class shall be entitled, to the extent only of their respective unpaid balances, to share in the general estate with general creditors. In, or for the purpose of, distributing such fund, all property other than cash shall be valued as of the close of business on the filing date. To the greatest extent considered practicable by the trustee, the trustee shall deliver in payment of claims of customers for their net equities based upon securities held on the filing date in their accounts (after giving effect to open contractual commitments completed as hereinafter provided), securities of the same class and series of an issuer ratably up to the respective amounts which were so held in such accounts. Any property remaining after the liquidation of a lien or pledge made by a debtor shall be apportioned between his general estate and the single and separate fund in the proportion in which the general property of the debtor and the property of his customers contributed to such lien or pledge.

(C) Specifically identifiable property.—The trustee shall return specifically identifiable property to the customers of the debtor, entitled thereto. No cash or securities at any time received, acquired, or held by or for the account of a debtor from or for the accounts of customers shall for the purposes of this paragraph be deemed to be specifically identified, unless such property remained in its identical form in the debtor's possession until the filing date, or unless such property was allocated to or physically set aside for such customers on the filing date. In determining whether property was allocated to or physically set aside for such customers, it shall be sufficient that on the filing date:

(i) securities are segregated individually, or in bulk for customers collectively;

(ii) in the case of securities held for the account of the debtor as part of any central certificate service of any clearing corporation or any similar depositary—

(I) the records of the debtor show or there is otherwise established to the satisfaction of the trustee that all or a specified part of the securities held by such clearing corporation or other similar depositary are held for specified customers, or for customers collectively, and

(II) such records of the debtor also show or there is otherwise established to the satisfaction of the trustee the identities of the particular customers entitled to receive specified numbers or units of such securities so held for customers collectively; or

(iii) such property is held for the account of customers of the debtor in such other manner as the Commission, for the protection of customers and other creditors on a fair and equitable basis, by rule or regulation shall have determined to be sufficiently identifiable as the property of such customers.

If there is any shortage in securities of the same class and series of an issuer so segregated in bulk or otherwise held for customers pursuant to this subparagraph, as compared to the aggregate rights of particular customers to receive securities of such class and series, the respective interests of such customers in such securities and such class and series shall be prorated, without prejudice, however, to the satisfaction of any claim for deficiencies as otherwise provided in this section.

(D) Where such single and separate fund is not sufficient to pay in full the claims of such single and separate class of creditors, a transfer by a debtor of any property which, except for such transfer, would have been a part of such fund may be recovered by the trustee for the benefit of such fund, if such transfer is voidable or void under the provisions of the Bankruptcy Act [*11 U.S.C.A. §§ 1* et seq.]. For the purpose of such recovery, the property so transferred shall be deemed to have been the property of the debtor and, if such transfer was made to a customer or for his benefit, such customer shall be deemed to have been a creditor, the laws of any State to the contrary notwithstanding. Subject to the provisions of paragraph (D), if any securities received or acquired by a debtor from a cash customer are transferred by the debtor, such customer shall not have any specific interest in or specific right to any securities of like kind on hand on the filing date, but such securities of like kind or the proceeds thereof shall become part of such single and separate fund.

(d) Completion of open contractual commitments.—The trustee shall complete those contractual commitments of the debtor relating to transactions in securities which were made in the ordinary course of debtor's business and which were outstanding on the filing date—

(1) in which a customer had an interest, except those commitments the completion of which the Commission shall have determined by rule or regulation not to be in the public interest, or

(2) in which a customer did not have an interest, to the extent that the Commission shall by rule or regulation have determined the completion of such commitments to be in the public interest.

For purposes of this subsection (but not for any other purpose of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]

(i) the term "customer" means any person other than a broker or dealer, and

(ii) a customer shall be deemed to have had an interest in a transaction if a broker participating in the transaction was acting as agent for a customer, or if a dealer participating in the transaction held a customer's order which was to be executed as a part of the transaction. All property at any time received, acquired, or held by or for the account of the debtor (except for cash or securities that are specifically identifiable as the property of particular customers and are not the subject of an open contractual commitment), and all property in the single and separate fund, shall be available to complete open contractual commitments pursuant to this subsection. Securities purchased or cash received by the trustee upon completion of any such commitment shall constitute specifically identifiable property of a customer to the extent that such commitment was completed with property which constituted specifically identifiable property of such customer on the filing date, or was paid or delivered by or for the account of such customer to the debtor or the trustee after the filing date.

(e) Notice.—Promptly after his appointment, the trustee shall cause notice of the commencement of proceedings under this section to be published in accordance with a designation of the court, made in accordance with the requirements of section 28 of the Bankruptcy Act [*11 U.S.C.A. § 51],* and at the same time shall cause to be mailed a copy of such notice to each of the customers of the debtor as their addresses shall appear from the debtor's books and records. Except as the

trustee may otherwise permit, claims for specifically identifiable property (other than securities registered in the name of the claimant or segregated for him in his individual name) or claims payable from property in the single and separate fund or payable with moneys advanced by SIPC, shall not be paid other than from the general estate of the debtor unless filed within such period of time (not exceeding sixty days after such publication) as may be fixed by the court, and no claim shall be allowed after the time specified in section 57 of the Bankruptcy Act [*11 U.S.C.A. § 93]*. Subject to the foregoing, and without limiting the powers and duties of the trustee to discharge promptly obligations as specified in this section, the court may make appropriate provision for proof and enforcement of all claims against the debtor including those of any subrogee.

(f) SIPC advances to trustee.—

(1) Advances for customer's claims.—In order to provide for prompt payment and satisfaction of the net equities of customers of debtor, SIPC shall advance to the trustee such moneys as may be required to pay or otherwise satisfy claims in full of each customer, but not to exceed $50,000 for such customer; except that—

(A) insofar as all or any portion of the net equity of a customer is a claim for cash, as distinct from securities, the amount advanced by reason of such claim to cash shall not exceed $20,000;

(B) a customer who holds accounts with the debtor in separate capacities shall be deemed to be a different customer in each capacity;

(C) no such advance shall be made by SIPC to the trustee to pay or otherwise satisfy, directly or indirectly, any claims of a customer who is a general partner, officer, or director of the debtor, the beneficial owner of 5 per centum or more of any class of equity security of the debtor (other than a nonconvertible stock having fixed preferential dividend and liquidation rights) or limited partner with a participation of 5 per centum or more in the net assets or net profits of the debtor; and

(D) no such advance shall be made by SIPC to the trustee to pay or otherwise satisfy claims of any customer who is a broker or dealer or bank other than to the extent that it shall be estimated to the satisfaction of the trustee, from the books and records of the debtor or from the books and records of a broker or dealer or bank or otherwise, that claims of such broker or dealer or bank against the debtor arise out of transactions for customers of such broker or dealer or bank, in which event, each such customer of such broker or dealer or bank shall be deemed a separate customer of the debtor. To the extent that moneys are advanced by SIPC to the trustee to pay the claims of customers, SIPC shall be subrogated to the claims of such customers with the rights and priorities provided in this section.

(2) Other advances.—SIPC may advance to the trustee such moneys as may be required to effectuate subsection (b)(1)(A). SIPC shall advance to the trustee such moneys as (with those available pursuant to subsection (d)) may be required to effectuate subsection (d).

(g) Payments to customers.—No proof of claim required.—It shall be the duty of the trustee to discharge promptly, in accordance with the provisions of this section, all obligations of the debtor to each of its customers relating to, or net equities based upon, securities or cash by the delivery of securities or the effecting of payments to such customer (subject to subsection (f)(1), to the extent that such payments are made out of advances from SIPC under such subsection) insofar as such obligations are ascertainable from the books and records of the debtor or are otherwise established to the satisfaction of the trustee, whether or not such customer shall have filed formal proof of such claim. For that purpose the court among other things shall—

(1) in respect of claims relating to securities or cash, authorize the trustee to make payment out of moneys made available to the trustee by SIPC notwithstanding the fact that there shall not have been any showing or determination that there are sufficient funds of the debtor available to make such payment; and

(2) in respect of claims relating to, or net equities based upon, securities of a class and series of an issuer, which are ascertainable from the books and records of the debtor or are otherwise established to the satisfaction of the trustee, authorize the trustee to deliver securities of such class and series if and to the extent available to satisfy such claims in whole or in part, with partial deliveries to be made pro rata to the greatest extent considered practicable by the trustee.

Any payment or delivery of property pursuant to this subsection may be conditioned upon the trustee requiring claimants to execute in a form to be determined by the trustee, appropriate receipts, supporting affidavits, and assignments, but shall be without prejudice to the right of any claimant to file formal proof of claim within the period specified in subsection (e) for any balance of securities or cash to which he may deem himself entitled.

(h) Proof of claim by associates and others.—The provisions of this section permitting discharge of obligations of the debtor to pay cash or to deliver securities without formal proof of claim shall not apply to any person "associated" with the debtor as defined in section 3(a)(18) of the 1934 Act [*15 U.S.C.A. § 78c*(a)(18)], to any beneficial owner of 5 per centum or more of the voting stock of the debtor, or to any member of the immediate family of any of the foregoing.

(i) Reports by trustee to court.—All reports to the court by a trustee (other than reports required to be filed pursuant to section 167(3) of the Bankruptcy Act [*11 U.S.C.A. § 567*(3)]) shall be in such form and detail as, having due regard

to the requirements of section 17 of the 1934 Act [*15 U.S.C.A. § 78q]* and the rules and regulations thereunder and the magnitude of items and transactions involved in connection with the operations of a broker or dealer, the Commission shall determine by rules and regulations to present fairly the results of such proceeding as at the dates or for the periods covered by such reports.

(j) Effect of Act on claims.—Except as otherwise provided in this section, nothing in this section shall limit the right of any person to establish by formal proof such claims as such person may have to payment, or to delivery of specific securities, without resort to moneys advanced by SIPC to the trustee. (Dec. 30, 1970, P. L. 91–598 § 6, 84 Stat 1646.)

§ 78ggg. SEC functions.—

(a) Administrative procedure.—Determinations of the Commission, for purposes of making rules or regulations pursuant to section 3(e) and section 9(f) [*15 U.S.C.A. §§ 78ccc*(e), 78iii(f)] shall be after appropriate notice and opportunity for a hearing, and for submission of views of interested persons, in accordance with the rulemaking procedures specified in section 553 of title 5, United States Code [*5 U.S.C.A. § 553]*, but the holding of a hearing shall not prevent adoption of any such rule or regulation upon expiration of the notice period specified in subsection (d) of such section and shall not be required to be on a record within the meaning of subchapter II of chapter 5 of such title [*5 U.S.C.A. §§ 551*–559].

(b) Enforcement of actions.—In the event of the refusal of SIPC to commit its funds or otherwise to act for the protection of customers of any member of SIPC, the Commission may apply to the district court of the United States in which the principal office of SIPC is located for an order requiring SIPC to discharge its obligations under this Act and for such other relief as the court may deem appropriate to carry out the purposes of this Act.

(c) Examinations and reports.—

(1) Examination of SIPC.—The Commission may make such examinations and inspections of SIPC and require SIPC to furnish it with such reports and records or copies thereof as the Commission may consider necessary or appropriate in the public interest or to effectuate the purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll].

(2) Reports from SIPC.—As soon as practicable after the close of each fiscal year, SIPC shall submit to the Commission a written report relative to the conduct of its business, and the exercise of the other rights and powers granted by this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], during such fiscal year. Such report shall include financial statements setting forth the financial position of SIPC at the end of such fiscal year and the results of its operations (including the source and application of its funds) for such fiscal year. The financial statements so included shall be examined by an independent public accountant or firm of independent public accountants, selected by SIPC and satisfactory to the Commission, and shall be accompanied by the report thereon of such accountant or firm. The Commission shall transmit such report to the President and the Congress with such comment thereon as the Commission may deem appropriate. (Dec. 30, 1970, P. L. 91–598 § 7(a–c), 84 Stat 1652.)

§ 78hhh. Examining authority functions.—

Each member of SIPC shall file with such member's examining authority such information (including reports of, and information with respect to, the gross revenues from the securities business of such member, including the composition thereof, transactions in securities effected by such member, and other information with respect to such member's activities, whether in the securities business or otherwise, including customer accounts maintained, net capital employed, and activities conducted) as SIPC may determine to be necessary or appropriate for the purpose of making assessments under section 4 [*15 U.S.C.A. § 78ddd]*. The examining authority shall file with SIPC all or such part of such information (and such compilations and analyses thereof) as SIPC, by bylaw or rule, shall prescribe. No application, report, or document filed pursuant to this section shall be deemed to be filed pursuant to section 18 of the 1934 Act [*15 U.S.C.A. § 78r]*. (Dec. 30, 1970, P. L. 91–598 § 8, 84 Stat 1653.)

§ 78iii. Functions of self–regulatory organizations.—

(a) Collection agent.—Each self–regulatory organization shall act as collection agent for SIPC to collect the assessments payable by all members of SIPC for whom such self–regulatory organization is the examining authority, and members of SIPC who are not members of any self–regulatory organization shall make payment direct to SIPC. An examining authority shall be obligated to remit to SIPC assessments made under section 4 [*15 U.S.C.A. § 78ddd]* only to the extent that payments of such assessments are received by such examining authority.

(b) Immunity.—No self–regulatory organization shall have any liability to any person for any action taken or omitted in good faith pursuant to section 5(a)(1) [*15 U.S.C.A. § 78eee*(i)].

(c) Inspections.—The self–regulatory organization of which a member of SIPC is a member shall inspect or examine such member for compliance with applicable financial responsibility rules, except that if a member of SIPC is a member of more than one self–regulatory organization, SIPC shall designate one of such self–regulatory organizations to inspect or examine such member of SIPC for compliance with applicable financial responsibility rules. Such self–regulatory organization shall be selected by SIPC on the basis of regulatory procedures employed, availability of staff, convenience

of location, and such other factors as SIPC may consider appropriate for the protection of customers of its members.
(d) Reports.—There shall be filed with SIPC by the self-regulatory organizations such reports of inspections or examinations of the members of SIPC (or copies thereof) as may be designated by SIPC by bylaw or rule.
(e) Consultation.—SIPC shall consult and cooperate with the self-regulatory organizations toward the end:
(1) that there may be developed and carried into effect procedures reasonably designed to detect approaching financial difficulty upon the part of any member of SIPC;
(2) that, as nearly as may be practicable, examinations to ascertain whether members of SIPC are in compliance with applicable financial responsibility rules will be conducted by the self-regulatory organizations under appropriate standards (both as to method and scope) and reports of such examinations will, where appropriate, be standard in form; and
(3) that, as frequently as may be practicable under the circumstances, each member of SIPC will file financial information with, and be examined by, the self-regulatory organization which is the examining authority for such member.
(f) Financial condition of members.—Notwithstanding the limitations contained in sections 15A and 19 of the 1934 Act [*15 U.S.C.A. §§ 78o-3*, 78s] and without limiting its powers under those or other sections of the 1934 Act [*15 U.S.C.A. §§ 78a* et seq.], the Commission may by such rules or regulations as it determines to be necessary or appropriate in the public interest and to effectuate the purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll]—
(1) require any self-regulatory organization to adopt any specified alteration of or supplement to its rules, practices, and procedures with respect to the frequency and scope of inspections and examinations relating to the financial condition of members of such self-regulatory organization and the selection and qualification of examiners;
(2) require any self-regulatory organization to furnish SIPC and the Commission with reports and records or copies thereof relating to the financial condition of members of such self-regulatory organization; and
(3) require any self-regulatory organization to inspect or examine any members of such self-regulatory organization in relation to the financial condition of such members. In the case of a broker or dealer who is a member of more than one self-regulatory organization the Commission, to the extent practicable, shall avoid requiring duplication of examinations, inspections, and reports. (Dec. 30, 1970, P. L. 91-598 § 9, 84 Stat 1654.)
§ 78jjj. Prohibited acts.—
(a) Failure to pay assessment.—If a member of SIPC shall fail to file any report or information required pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll], or shall fail to pay when due all or any part of an assessment made upon such member pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll], and such failure shall not have been cured, by the filing of such report or information or by the making of such payment, together with interest thereon, within five days after receipt by such member of written notice of such failure given by or on behalf of SIPC, it shall be unlawful for such member, unless specifically authorized by the Commission, to engage in business as a broker or dealer. If such member denies that he owes all or any part of the amount specified in such notice, he may after payment of the full amount so specified commence an action against SIPC in the appropriate United States district court to recover the amount he denies owing.
(b) Engaging in business after appointment of trustee.—It shall be unlawful for any broker or dealer for whom a trustee has been appointed pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll] to engage thereafter in business as a broker or dealer, unless the Commission otherwise determines in the public interest. The Commission may by order bar or suspend for any period, any officer, director, general partner, owner or 10 per centum or more of the voting securities, or controlling person of any broker or dealer for whom a trustee has been appointed pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll] from being or becoming associated with a broker or dealer, if after appropriate notice and opportunity for hearing, the Commission shall determine such bar or suspension to be in the public interest.
(c) Embezzlement of assets of SIPC.—Whoever steals, unlawfully abstracts, unlawfully and willfully converts to his own use or to the use of another, or embezzles any of the moneys, securities, or other assets of SIPC shall be fined not more than $50,000 or imprisoned not more than five years or both. (Dec. 30, 1970, P. L. 91-598 § 10, 84 Stat 1655.)
§ 78kkk. Miscellaneous provisions.—
(a) Public inspection of reports.—Any notice, report, or other document filed with SIPC pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll] shall be available for public inspection unless SIPC or the Commission shall determine that disclosure thereof is not in the public interest. Nothing herein shall act to deny documents or information to the Congress of the United States or the committees of either House having jurisdiction over financial institutions, securities regulation, or related matters under the rules of each body. Nor shall the Commission be denied any document or information which the Commission, in its judgment, needs.
(b) Application of Act to foreign members.—Except as otherwise provided by rule or regulation of the Commission, if the head office of a member is located, and the member's principal business is conducted, outside the United States, the provisions of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa-78lll] shall apply to such member only in respect of the business

of such member conducted in the United States.

(c) Liability of members of SIPC.—Except for such assessments as may be made upon such member pursuant to provisions of section 4, no member of SIPC shall have any liability under this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll] as a member of SIPC for, or in connection with, any act or omission of any other broker or dealer whether in connection with the conduct of the business or affairs of such broker or dealer or otherwise and, without limiting the generality of the foregoing, no member shall have any liability for or in respect of and indebtedness or other liability of SIPC.

(d) Liability of SIPC and directors.—Neither SIPC nor any of its Directors shall have any liability to any person for any action taken or omitted in good faith under or in connection with any matter contemplated by this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll].

(e) Advertising.—SIPC shall by bylaw or rule prescribe the manner in which a member of SIPC may display any sign or signs (or include in any advertisement a statement) relating to the protection to customers and their accounts, or any other protections, afforded under this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]. No member may display any such sign, or include in an advertisement any such statement, except in accordance with such bylaws and rules.

(f) SIPC exempt from taxation.—SIPC, its property, its franchise, capital, reserves, surplus, and its income, shall be exempt from all taxation now or hereafter imposed by the United States or by any State or local taxing authority, except that any real property and any tangible personal property (other than cash and securities) of SIPC shall be subject to State and local taxation to the same extent according to its value as other real and tangible personal property is taxed. Assessments made upon a member of SIPC shall constitute ordinary and necessary expenses in carrying on the business of such member for the purpose of section 162(a) of the Internal Revenue Code of 1954 [*26 U.S.C.A. § 162*(a)]. The contribution and transfer to SIPC of funds or securities held by any trust established by a national securities exchange prior to January 1, 1970, for the purpose of providing assistance to customers of members of such exchange, shall not result in any taxable gain to such trust or give rise to any taxable income to any member of SIPC under any provision of the Internal Revenue Code of 1954, nor shall such contribution or transfer, or any reduction in assessments made pursuant to this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll], in any way affect the status, as ordinary and necessary expenses under section 162(a) of the Internal Revenue Code of 1954 [*26 U.S.C.A. § 162*(a)], or any contributions made to such trust by such exchange at any time prior to such transfer. Upon dissolution of SIPC, none of its net assets shall inure to the benefit of any of its members.

(g) Section 20(a) of 1934 Act not to apply.—The provisions of subsection (a) of section 20 of the 1934 Act [*15 U.S.C.A. § 78t*(a)] shall not apply to any liability under or in connection with this Act.

(h) SEC study of unsafe or unsound practices.—Not later than twelve months after the date of enactment of this Act [Dec. 30, 1970], the Commission shall compile a list of unsafe or unsound practices by members of SIPC in conducting their business and report to the Congress (1) the steps being taken under the authority of existing law to eliminate those practices and (2) recommendations concerning additional legislation which may be needed to eliminate those unsafe or unsound practices. (Dec. 30, 1970, P. L. 91–598 § 11, 84 Stat 1655.)

§ 78lll. Definitions.—

For purposes of this Act [*15 U.S.C.A. §§ 78o*(c)(3), 78aaa–78lll]:

(1) Self–regulatory organization.—The term "self–regulatory organization" means a national securities exchange or a national securities association registered pursuant to subsection (b) of section 15A of the 1934 Act [*15 U.S.C.A. § 78o–3]*.

(2) Financial responsibility rules.—The term "financial responsibility rules" means the rules and regulations pertaining to financial responsibility and related practices which are applicable to a broker or dealer, as prescribed by the Commission under subsection (c)(3) of section 15 of the 1934 Act [*15 U.S.C.A. § 78o*(c)(3)] or prescribed by a national securities exchange.

(3) Examining authority.—The term "examining authority" means, with respect to any member of SIPC, the self–regulatory organization which inspects or examines such member of SIPC or the Commission if such member of SIPC is not a member of any self–regulatory organization. (Dec. 30, 1970, P. L. 91–598 § 12, 84 Stat 1956.)

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The Securities Investor Protection Act was substantially amended by P.L. 95–283, 92 Stat. 249, May 21, 1978; and by P.L. 95–598, 92 Stat. 2675, November 6, 1978. For details of these amendments, consult U.S.C.A.

[*2] Summary and comment

[*2a] Generally

Observing that serious and persistent financial problems which beset the securities industry in 1969–1970 had led to voluntary liquidations, mergers, receiverships, and bankruptcies of a substantial number of brokerage houses, and that since brokers often hold large amounts of money and securities for customers, such failures might lead to extensive customer losses, with concomitant weakening of confidence in the securities markets and adverse effects on the entire economy, Congress enacted the Securities Investor Protection Act of 1970 *(15 U.S.C.A. §§ 78aaa–*78lll) to alleviate the problems so recognized (HR No. 91–1613 (1970) US Code Cong & Adm News 5254).

It is clear, both from the legislative history of the SIPA (HR No. 91–1613, supra) and from judicial decisions (§ 3 , infra), that the primary purpose of the Act is to protect customers of securities broker–dealers from losses resulting from insolvency or financial instability of the broker–dealers. A secondary purpose has been said to be to stem the growing loss of public confidence in the ability of the brokerage industry to protect customer accounts (§ 3 , infra). Although it is the purpose of the Act to protect customers, not broker–dealers, the Act's protection has been extended to broker–dealers to a limited extent, where it was deemed appropriate for the ultimate protection of the investing public; thus, it has been said that in order to prevent the "domino effect," the insolvency of one broker–dealer bringing about the failure of other broker–dealers, the Act calls for the completion of open contractual commitments between an insolvent broker–dealer and other broker–dealers where customers have an interest in those open commitments (§ 21[b] , infra).

To accomplish its purpose, the SIPA calls for the establishment of a fund *(15 U.S.C.A. § 78ddd)* from which customers of an insolvent broker–dealer, whose assets are insufficient to satisfy its financial obligations to its customers, may obtain payment of their claims up to $50,000 per customer *(15 U.S.C.A. § 28fff*(g)). The Act creates the Securities Investor Protection Corporation to administer the fund and to insure that customers of insolvent broker–dealers receive the protection of the Act *(15 U.S.C.A. § 78ccc).* The SIPC is a nonprofit corporation having as its members all broker–dealers registered under the Securities Exchange Act of 1934, and, with limited statutory exceptions *(15 U.S.C.A. § 78ccc*(a)(2)), all members of national securities exchanges. Other broker–dealers may become members on a voluntary basis under conditions established by the SIPC *(15 U.S.C.A. § 78ccc*(f)). The basic source of the fund established (SIPC fund) is member assessments *(15 U.S.C.A. § 78ddd*(c)).

Upon its determination that a broker–dealer is in danger of failing to meet its financial obligations, and that the customers of the broker–dealer are in need of the protection of the Act, the SIPC may petition a Federal District Court for the appointment of a trustee *(15 U.S.C.A. § 78eee*(a)(2)) and the liquidation of the broker–dealer's business *(15 U.S.C.A. § 78fff).* When appointed, the trustee is required to return specifically identifiable property to customers of the debtor *(15 U.S.C.A. § 78fff*(c)(2)(C)), complete open contractual commitments covered by the Act *(15 U.S.C.A. § 78fff*(d)), distribute the "single and separate fund" (proceeds of all customers' property transferred by the debtor) ratably to customers *(15 U.S.C.A. § 78fff*(c)(2)(B)), and pay off, with money from the SIPC fund, remaining debts owed to customers, to the extent provided by the Act *(15 U.S.C.A. § 78fff*(g)). The Act also provides that in the event that the SIPC may refuse to act under the SIPA, the Securities and Exchange Commission may apply to a District Court to require the SIPC to discharge its obligations under the Act *(15 U.S.C.A. § 78ggg*(b)).

To the limited extent that the constitutionality of the Act has been challenged, it generally has been held to be valid (§ 4 , infra). In this regard, it has been held that the fact that the SIPC is not required to afford a broker–dealer a hearing prior to petitioning the court for the appointment of a trustee does not violate the broker–dealer's right to due process, provided that the Act is interpreted to require the District Court to make a de novo determination of the need for customer protection (§§ 4 10[a] , infra). Where a broker–dealer had ample opportunity to present his evidence, and to argue that the evidence failed to show that it was in danger of failing to meet its obligations, it was held that the judicial hearing adequately satisfied requirements in this respect (§ 10[b] , infra). It also has been held that it does not violate a broker–dealer's constitutional rights to interpret the Act so as not to allow for payment, out of the estate or SIPC funds, of attorney's fees incurred by the broker–dealer in resisting the appointment of a trustee (§ 4 , infra). And it has been held, in response to a challenge to the constitutionality of the Act, that there is a rational basis for the "single and separate fund" concept contained within the Act (§ 4 , infra).

It has been held that Congress intended the Act to apply prospectively only, and that its protection does not apply to customers of broker–dealers who went out of business prior to the effective date of the Act. Thus, the Act has been held inapplicable where a broker–dealer had effectively ceased doing business as such by the critical date, notwithstanding that his registration with the SEC as a broker–dealer may have continued beyond that date (§ 5 , infra).

The decisions are not uniform as to whether customers of a broker–dealer, or those acting on behalf of such customers, have standing to compel the SIPC to take action under the Act, or whether such standing is limited to the SEC. On the

one hand, it has been held that only the SEC may so act, the SIPC's powers being said to be discretionary except when it is required to act pursuant to a court order initiated by the Commission. On the other hand, it has been held that a receiver appointed for an insolvent broker–dealer, acting on behalf of the broker–dealer's customers, had standing to bring action to invoke the provisions of the SIPA (§ 6 , infra).

Liquidation proceedings under the Act generally proceed in accordance with the provisions of Chapter X of the Bankruptcy Act, which are expressly incorporated in the SIPA except to the extent that they may be inconsistent with the SIPA. It has been held that a provision of the Bankruptcy Act is inconsistent with the SIPA only if it conflicts with an explicit provision of the Act or if its application would substantially impede the fair and effective operation of the SIPA without providing countervailing benefits, and that a provision of the Bankruptcy Act is not inconsistent, merely because it is not absolutely necessary for the operation of the Act (§ 7 , infra). Although federal courts generally have summary jurisdiction in Chapter X proceedings, it has been said that such jurisdiction does not exist where a liquidation is ordered and, therefore, since SIPA proceedings are liquidation proceedings, summary jurisdiction also is absent in those proceedings (§ 8 , infra).

It has been concluded that in order properly to determine that customers of a broker–dealer are in need of protection of the SIPA, a District Court need find not only the existence of at least one of the five conditions specified in *15 U.S.C.A. § 78eee*(b)(1)(A), but in addition, under *15 U.S.C.A. § 78eee*(a)(2), that the broker–dealer has failed or is in danger of failing to meet its obligations to its customers (§ 9 , infra). It has been held that a finding that a broker–dealer was in danger of failing to meet its obligations to its customers was adequately supported by the evidence, where a principal stockholder of the brokerage had diverted $100,000 of a customer's money for his own use, where customers' securities were unlawfully hypothecated, and where a fiscal agent, appointed by the court, reported that the records of the broker–dealer were too misleading and inaccurate to be of any value in determining whether the broker–dealer had violated any securities laws (§ 11[a] , infra). Also, it was held that two of the conditions specified in *15 U.S.C.A. § 78eee*(b)(1)(A) were properly found to have been met where (1) the court's conclusion that the broker–dealer was unable to make such computations as may have been necessary to establish compliance with financial responsibility and hypothecation rules, was supported by a report of a special fiscal agent appointed by the court, and by information provided by an accounting firm hired by the fiscal agent to audit the broker–dealer's books; and (2) the court found that the broker–dealer was the subject of a pending court proceeding in which a receiver had been appointed for the broker–dealer, the court itself having appointed a receiver for the broker–dealer (§ 11[b] , infra).

Pursuant to the SIPA requirement that the trustee and the attorney for the trustee appointed under the Act be "disinterested," it has been held that where the SIPC nominated as trustee an individual who was a member of a law firm which regularly represented a major creditor of the debtor, and where the attorney nominated was the same law firm, the nominees did not meet the requirement of disinterestedness and were not qualified to serve in those capacities (§ 12 , infra).

With respect to the administration of an estate in liquidation under the SIPA, it has been held that securities received by the trustee after the filing date are not a part of the estate even though they were indorsed to the insolvent broker–dealer and mailed prior to that date, since title passes only upon delivery (§ 13 , infra). A trustee's request for a blanket extension of time for filing claims in SIPA liquidation proceedings has been denied where there was no showing that each late claim was meritorious and that the delay in filing was excusable (§ 14 , infra). Where a broker–dealer leased property prior to the initiation of liquidation proceedings and the receiver and trustee subsequently used that property while conducting the liquidation, it was held that the lessor had a priority claim for rental for the period during which the property was used by the receiver and trustee (§ 15 , infra). And the personal assets of a sole proprietor broker–dealer have been held to be includible in the assets available to the trustee for liquidation under the SIPA (§ 17 , infra).

It has been held that unlawful conduct on the part of an SIPA claimant, with respect to the circumstances upon which a claim is based, will make the protection of the Act unavailable to the claimant. Thus, where a claimant had conspired with the insolvent broker–dealer to manipulate the price of securities, it was held that the claimant's criminal conduct and the "clean hands" doctrine barred recovery under the Act. And where a claimant knowingly violated the margin regulations in a transaction upon which his claim was based, he was held to be ineligible for recovery (§ 16 , infra).

Since the SIPA is designed to protect "customers" of broker–dealers, it has sometimes been necessary to determine who are "customers" within the meaning of the Act. For example, it has been held that a voluntary lender of securities to a failing brokerage firm was not a "customer" of the firm by virtue of that loan, and that since the Act was designed to protect investors, the lender would so qualify only if the loan was made with the intent to use the securities in some

type of securities trading or investment activity. It has been said that if a broker–dealer, with authorization, sold securities owned by another person, and used the proceeds to make unauthorized purchases of different securities, the person whose securities were sold would be a "customer" under the Act, but where it was found that the purchase of the different securities was authorized, it has been held that the person authorizing the purchase did not have a "customer's claim" for the proceeds of the sale of the first securities, even though the authorization may have been obtained through fraud; such a person's fraud claim has been said to be the claim of a general creditor to be satisfied out of the broker–dealer's general estate. And it has been concluded that where a broker–dealer agrees to purchase securities, the seller becomes a customer only upon actual delivery of the securities to the broker–dealer, and that where delivery is not effected, the seller does not have a customer's claim under the Act, and his claim is that of an unsecured creditor, based upon the broker–dealer's breach of contract, against the broker–dealer's general estate (§ 18 , infra).

A customer's "net equity" with a broker–dealer, which is to be paid out of the single and separate fund or the SIPC fund under the Act, has been held to consist of both his cash balance and his securities account with the broker–dealer. Thus, where a broker–dealer received payment from a customer for shares of a prospective new issue, but went into liquidation under the Act without delivering the shares, it was held that if, under applicable law or regulations, the broker–dealer was obligated to reimburse the customer the money so received, that amount was required to be included in the customer's net equity. However, where a broker–dealer had transmitted customers' funds to banks in payment for certificates of deposit, it being understood that the banks were to send the certificates directly to the customers, but where the banks were placed in receivership without having done so, and the broker–dealer was placed in liquidation under the Act, the funds which had been transmitted to the bank were held not includible in the customers' net equity in the broker–dealer's estate, since there was no further action to be taken by the broker–dealer (§ 19 , infra).

Where a customer's net equity claim has been found to be a cash claim, payment out of the SIPC fund has been held subject to the limitation expressly provided by the Act (§ 20 , infra).

"Open contractual commitments" which, under the SIPA, are required to be completed by the trustee have been held to include only those between the insolvent broker–dealer and other broker–dealers; open contractual commitments between the debtor and a customer have been held not included (§ 21[b] , infra). Moreover, pursuant to the statutory provisions pertaining to "open contractual commitments," the SEC has promulgated a rule (17 CFR § 240.206d–1) stating under what circumstances the trustee's completion of such commitments is or is not "in the public interest" (§ 21[a] , infra).

Where a broker–dealer purchases and actually receives stock on behalf of a customer, that stock has been held to be "specifically identifiable property" which must be delivered to the customer in a liquidation proceeding under the SIPA, but the particular stock identifiable to the customer must have been received by the broker–dealer; the customer does not have the right to receive shares of the same class obtained for other customers, or to share in the proceeds of the sale of such other shares. Specifically identifiable property has also been held to include funds which have been allocated to a customer; thus, where a broker–dealer sent a check to a customer in intended settlement of the customer's credit balance, but the customer did not cash the check, the customer was held entitled, in a subsequent SIPA liquidation of the broker–dealer's business, to receive the amount of the check as specifically identifiable property. However, a customer has been held to have the right to receive specifically identifiable property only where he has the immediate right to possession of the property, and it has been held that if the customer has not fully paid for securities, they may not be delivered to him as specifically identifiable property (§ 22 , infra).

It has been held that fees awarded to a trustee or his attorney under the SIPA must be reasonable, and that in fixing such fees, a court may take into account such factors as the nature and complexity of the work involved and the magnitude of the estate and claims. Also it has been held that the fees awarded should not include payment for background research relating to the securities industry and applicable law, since the court has the right to presume that familiarity with the appropriate area of the law was a factor in the nomination of the trustee and counsel. And it has been held that fees should not be granted for work done prior to the appointments of the trustee and counsel. Moreover, it has been said that the court is not bound by the SIPC's approval of the fees requested, and that such approval carries no weight where it appears that the SIPC has not examined the requests closely. It also has been held that in establishing fees for trustees and their attorneys under the SIPA, the "going rate" for attorneys in the geographical area is not necessarily the standard to be applied, particularly in a routine liquidation principally involving accounting determinations of the net equities of the debtor's customers (§ 23[a] , infra).

It has been held that ordinarily trustees and their attorneys should not be awarded interim fees in liquidation proceedings under the SIPA, the proper time for determining those fees being the time of completion of the administration

of the estate (§ 23[b] , infra).

It has been held that an attorney, who represents a broker–dealer in resisting the appointment of a trustee for the liquidation under the SIPA, of the broker–dealer's business, cannot have his fee paid from the liquidation estate or from the SIPC fund, since resisting liquidation is not a purpose of the liquidation proceeding and the Act therefore does not provide for payment for such activities (§ 24[a] , infra). However, it has been held that an attorney for a claimant may have a priority claim for the value of his services under the SIPA where his efforts have benefitted the estate; thus, the successful appeal of the disallowance of a claim of an attorney's client was held to have benefitted the estate, and fees for such legal services were held allowable under the Act, where the client and others similarly situated properly received payments that they would not have received had the appeal not been prosecuted, it being said to be of benefit to the estate to have the law adhered to rather than violated (§ 24[b] , infra).

[*2b] Practice pointers

Where a claim against a brokerage firm cannot be maintained under the SIPA, or where it is not possible to obtain full recovery, it may, nevertheless, be worthwhile, where the claim is based upon violation of the Securities Act or the Securities Exchange Act, to seek to recover from individuals in control of the firm. For example, § 15 of the Securities Act *(15 U.S.C.A. § 77o)* provides that where a person becomes liable to another person under the provisions of the Act, any person who controls the liable person shall be jointly and severally liable with the controlled person, unless the controlling person has no knowledge of or reasonable grounds to believe in the existence of the facts upon which the controlled person's liability is based. A similar provision in § 20a of the Securities Exchange Act *(15 U.S.C.A. § 78t*(a)) provides that a controlling person shall be civilly liable, jointly and severally, with a controlled person by reason of the controlled person's violation of the Exchange Act, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action. As used in the Securities Act *(15 U.S.C.A. § 77b*(2)) and the Exchange Act *(15 U.S.C.A. § 78c*(9)), the term "person" includes corporations and partnerships; thus, persons in control of a corporation, such as directors, may be liable for violations of the securities laws which are attributable to the corporation. (See *Moerman v Zipco, Inc. (1969, DC NY) 302 F Supp 439,* affd (CA2 NY) *422 F2d 871,* adhered to (CA2 NY) *430 F2d 362 ; Schamber v Aaberg (1960, DC Colo) 186 F Supp 52* .) Similarly, it has been held that under § 15 of the Securities Act, partners of a brokerage firm were liable for misrepresentations of an employee in connection with the sale of securities. (See *Johns Hopkins University v Hutton (1970, CA4 Md) 422 F2d 1124.)*

Although, with limited statutory exceptions, any broker–dealer who is registered under the Securities Exchange Act or who is a member of a national securities exchange is automatically a member of the SIPC *(15 U.S.C.A. § 78ccc*(A)(2)), failure to meet obligations of SIPC membership will not affect the broker–dealer's status as a broker–dealer with respect to application of the Securities Exchange Act. Thus, in Securities & Exchange Com. v Midland Equity Corp. (1973, DC NY) *CCH Fed Secur L Rep P 94305,* the court rejected the argument that failure by a broker–dealer to pay its SIPC assessment or to otherwise comply with the provisions of the SIPA placed the broker beyond the reach of the SEC's power of inspection or otherwise affected his status as a broker–dealer within the meaning of the Securities Exchange Act. In defending against an SEC motion for an order restraining the broker–dealer and its principal officer from continued violations of the visitation and inspection provisions of the federal securities laws, the broker–dealer asserted that he was no longer a broker–dealer since he had received a letter from the SIPC stating that his brokerage house had failed to pay its SIPC assessment for a specified year. The court stated that the broker–dealer relied upon the theory that its failure to pay its assessment in some manner effectuated a withdrawal of its registration as a broker–dealer, its failing to comply with the provisions of the SIPA placing it beyond the reach of the SEC's power of inspection, but the court concluded that such an argument was clearly without merit. Conversely, the SEC has declared, in Re Garofolo (1971, SEC) *CCH Fed Secur L Rep, P 78495,* that the revocation of a broker–dealer's registration and his expulsion from the National Association of Securities Dealers should not affect a trustee appointed to liquidate the broker–dealer's business under the SIPA in the performance of his functions under the SIPA.

Counsel should be aware that the filing of timely written objections may be necessary if he intends, on behalf of his client, to oppose the plan of a trustee in an SIPA liquidation. In *Securities & Exchange Com. v Milner (1973, CA1 Mass) 474 F2d 162,* the Court of Appeals affirmed the District Court's refusal to entertain oral objections to a plan where no written objections had been filed. The court pointed out that there had been two District Court hearings, the first having been preceded by written notice formulated and mailed pursuant to court order and received approximately one month before the hearing, accompanied by a copy of the plan and providing for a creditors' meeting. The notice stated that objections to the plan were to be filed in writing with the District Court within 10 days after the creditors' meeting, and

that the hearing would be on any objections to the plan which had been timely filed. The Court of Appeals stated that written objections not only focus the court's attention, but in a proceeding such as the one before the court, give the trustee and other creditors fair notice of matters they may wish to answer. The court added that District Courts are not required to entertain vague, unformulated protests from attorneys and clients who disregard clear and patently reasonable advance instructions to reduce their complaints to writing.

In advising broker–dealer clients regarding compliance with the SIPA, counsel should be aware of the SEC's adoption of an Amendment to SEC Rule 17a–5 (17 CFR § 240.17a–5). The Amendment added a new subparagraph ((b)(4)) to the Rule, requiring each report filed by a broker–dealer pursuant to Rule 17a–5 to be accompanied by a supplemental report on the status of the broker–dealer's membership in the SIPC. Rule 17a–5 requires registered broker–dealers, and broker–dealers who are members of national securities exchanges, to file, with the SEC, annual financial reports, which usually are required to be certified. (For a discussion of financial reports required by the SEC to be filed by broker–dealers, see 69 Am Jur 2d, Securities Regulation—Federal, §§ 340, 341) The supplemental report, required by subparagraph (b)(4), consists of a schedule detailing SIPC assessment payments and overpayments applied or carried forward to future use, or in the alternative, a statement that the broker–dealer is a person not required to be an SIPC member by virtue of the provisions of the SIPA. The supplemental report must be accompanied by a report of the independent public accountant, who certified the annual report of the broker–dealer, to the effect that the assessment payments were determined fairly and in accordance with applicable instructions and forms, or that claim for exclusion from membership was consistent with income reported. The Rule further calls for a statement by the accountant as to any corrective action taken, or proposed to be taken, by the broker–dealer with regard to any exception noted by the accountant.

[*II] General considerations

[*3] Purpose of Act

In the following cases, the courts have discussed the purpose of the SIPA, generally holding that its principal purpose is the protection of securities investors from losses resulting from financial problems encountered by their brokers or dealers.

Primary purpose of Securities Investor Protection Act is protection of investors: Congress enacted Securities Investor Protection Act of 1970 *(15 U.S.C.A. §§ 78aaa* et seq.) to arrest failure or instability of significant number of brokerage firms, to restore investor confidence in capital markets, and to upgrade financial responsibility requirements for registered brokers and dealers. *Securities Investor Protection Corp. v Barbour 421 US 412, 44 L Ed 263, 95 S Ct 1733.*

The court stated that the purpose of the SIPA was to protect investors against losses caused by the insolvency of broker–dealers and not by the insolvency of the companies in which their funds had been invested, in *Securities & Exchange Com. v C. H. Wagner & Co. (1974, DC Mass) 373 F Supp 1214,* where the court, in overruling objections of customers of an insolvent broker to the trustee's disallowance of their claims, pointed out that their losses stemmed from the bankruptcy of the issuers of the certificates of deposits and letters of credit, which the customers had purchased through the broker, and that while the customers may have had quasi–contractual claims provable against the broker's general estate, they did not have preferred claims under the SIPA.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144,* a case dealing with the propriety of a District Court order adjudicating that the customers of a registered broker–dealer were in need of the protection provided by the Act, the court stated that the primary purpose of the Act is to afford protection to public customers in the event broker–dealers with whom they transact business encounter financial difficulties and are unable to satisfy their obligations to their public customers. The court added that the Act does not contemplate action by the SIPC unless there is a danger that the broker–dealer may not meet its obligations to its customers.

In *Securities & Exchange Com. v F. O. Baroff Co. (1974, CA2 NY) 497 F2d 280,* the court stated that the object of the SIPA, and the function of the SIPC therein created, was to protect the public customers of securities dealers from suffering the consequences of financial instability in the brokerage industry, the court upholding the rejection of the claim of a person who had lent securities to a brokerage firm which was subsequently liquidated under the Act, it being found that such lender was not a customer within the meaning of the Act.

The court stated that the objective of the SIPA was to protect members of the investing public, not brokers, in *Securities & Exchange Com. v Packer, Wilbur & Co. (1974, CA2 NY) 498 F2d 978,* where the court refused to honor a broker's claim against an insolvent broker, under the Act, as an open contractual commitment, because the claimant did

not represent a customer of the insolvent broker with respect to that claim.

In enacting Securities Investor Protection Act, Congress intended to protect public customer as investor and trader, not others who might become creditors of broker–dealer for independent reasons. *Securities Investor Protection Corp. v Executive Secur. Corp. (CA2 NY) 556 F2d 98.*

In *Securities Investor Protection Corp. v Charisma Secur. Corp. (1972, DC NY) 352 F Supp 302,* involving an application for an interim fee allowance to the trustee and counsel for the trustee serving in the liquidation of a brokerage house pursuant to the provisions of the SIPA, the court, noting that the SIPA had its genesis in the concern over the loss of public confidence in the brokerage industry due to the inability of the industry to adequately protect investors where broker–dealers with whom they were doing business encountered financial trouble, stated that the fund established by the Act, permitting customers to recover at least a part of their losses suffered in dealing with such broker–dealers, was intended to reinforce the confidence that investors have had in the United States securities market and to strengthen the financial responsibilities of broker–dealers.

In *Securities & Exchange Com. v Packer, Wilbur & Co. (1973, DC NY) 362 F Supp 510,* affd (CA2) *498 F2d 978,* an action involving the right to reimbursement from SIPC funds, the court stated that the Securities Investor Protection Act of 1970 was enacted to stem the growing loss of confidence of public investors in the ability of the brokerage industry to protect customer accounts and to generally strengthen the financial responsibility of broker–dealers so as to eliminate, to the maximum extent possible, risks which lead to customer loss. The court added that the Act seeks to insulate the securities market from any domino effect which may result from the failure of a brokerage house. The court pointed out that the Act was specifically intended to protect the innocent investor, not one who had engaged in a fraudulent transaction, the objective of SIPA being to reimburse an innocent customer for loss sustained.

In Handelman v Weiss (1973, DC NY) *CCH Fed Secur L Rep P 94214,* an action in which the plaintiff sought to recover for alleged violations of the antifraud provisions of the Federal Securities Laws, the court noted, in passing, that the SIPA was enacted in response to the financial crisis of 1969–70 which had led to the failure of several brokerage firms, such failure resulting in extensive customer losses, and that, as part of its efforts to protect the public investor, Congress, through the Act, created the SIPC to administer an insurance program designed to protect the customers of securities broker–dealers.

The court stated that the principal purpose of the SIPA was to protect investors against financial losses arising from the insolvency of their brokers, in *Securities & Exchange Com. v S. J. Salmon & Co. (1974, DC NY) 375 F Supp 867,* where the court affirmed the denial of a customer's claim, under the Act, based upon alleged fraud on the part of the insolvent broker. The court stated that the statutory scheme was designed to facilitate the return of property of customers of insolvent brokerage firms or, where that could not be done, to reimburse such customers if their property had been lost or misappropriated.

In *Securities & Exchange Com. v Capital Counsellors, Inc. (1974, DC NY) 378 F Supp 224,* an action wherein an attorney sought compensation for services rendered in opposition to the SEC's application for injunctive relief and receivership against an investment advisor, the court, in commenting on the SIPA, stated that the intendment of the Act was to protect customers of broker–dealers who had fallen into financial difficulty and who were incapable of meeting their customer obligations, the court further stating that imputation of fraud to the broker–dealer was unnecessary.

In *Rich v New York Stock Exchange (1974, DC NY) 379 F Supp 1122,* where an investor alleged damages as the result of a brokerage being placed in liquidation under the SIPA because of the alleged failure of a registered national stock exchange properly to supervise a member, the court commented that the purpose of the Act was to protect a class of investors from loss, without regard to the presence or absence of wrongdoing as a cause of broker–dealer insolvency.

In Securities & Exchange Com. v Kelly, Andrews & Bradley, Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94881,* the court stated that the SIPA was enacted to protect public customers of securities dealers from the consequences of financial instability in the broker–dealer industry by assuring recovery to customers in the event of a broker–dealer's insolvency, the court affirming the disallowance of several claims on the grounds that they did not meet the requirements of the Act.

Purpose of Securities Investor Protection Act (SIPA) is to provide greater protection for customers of registered brokers and dealers. Securities Investor Protection Act of 1970, § 1(a), as amended, *15 U.S.C.A. §§ 78aaa* et seq. *In re Stratton Oakmont, Inc., 257 B.R. 644 (S.D.N.Y. 2001).*

In *Securities & Exchange Com. v Aberdeen Secur. Co. (1973, CA3 Del) 480 F2d 1121,* cert den *414 US 1111, 38 L Ed*

2d 738, 94 S Ct 841, the court stated that the intent of Congress to protect customers of financially distressed securities dealers was clear in the enactment of the SIPA, and that the Act had been passed in response to demands that Congress provide some assurance to investors that they would not suffer financial loss as a consequence of the bankruptcy of their stockbrokers, the court adding that the theory of the statute was to provide a type of protection for securities purchasers somewhat similar to that enjoyed by bank depositors under the Federal Deposit Insurance Corporation.

Securities Investor Protection Act was passed by Congress to provide protection to investors if broker–dealer with whom they are doing business should encounter financial difficulties; Section 6(c) of Securities Investor Protection Act *(15 U.S.C.A. § 78fff*(c)) is intended to make flexible Chapter X procedures available for SIPA liquidations, but not every provision of Chapter X have been incorporated into Act; only those provisions relating to procedures for conducting affairs of estate during bankruptcy administration, where not inconsistent with provisions of Act, have been incorporated. *Securities & Exchange Com. v Aberdeen Secur. Co. (CA3) 526 F2d 603.*

Securities Investor Protection Act was intended to provide protection for brokerage house customers somewhat similar to that afforded bank depositors by *Federal Deposit Insurance Corporation. Securities & Exchange Com. v Albert & Maguire Secur. Co. (CA3) 560 F2d 569.*

In holding that the SIPA did not violate the constitutional guarantee of due process, the court, in *Securities & Exchange Com. v Albert & Maguire Secur. Co. (1974, DC Pa) 378 F Supp 906,* stated that the purpose of the Act was primarily to protect the rights of customers of broker–dealers against inequities which had been shown to exist.

In defining those who qualify as "customers" under the Securities Investor Protection Act (SIPA), Congress intended to provide a measure of special protection for those that entrust cash or securities to brokers/dealers for purpose of trading and investing. Securities Investor Protection Act of 1970, § 16(2), as amended, *15 U.S.C.A. § 78*<emph type="if">lll<endemph type="if">(2). *In re First Interregional Equity Corp., 290 B.R. 265, Fed. Sec. L. Rep. (CCH) P 92297 (Bankr. D. N.J. 2003).*

The court stated that the SIPA was enacted in response to the need to protect customers of securities brokers and dealers which might fail and thereby jeopardize the cash and securities that customers had left on deposit with such firms, in *Securities & Exchange Com. v Guaranty Bond & Secur. Corp. (1974, CA6 Tenn) 496 F2d 145,* cert gr (US) *42 L Ed 2d 138, 95 S Ct 172,* where the court held that an insolvent broker had been engaging in the brokerage business as of the effective date of the Act and that the Act was therefore applicable to the insolvency proceedings of that broker.

The court in *Securities & Exchange Com. v Schreiber Bosse & Co. (1973, DC Ohio) 368 F Supp 24,* stated that the basic purpose of the SIPA was to afford protection to public customers in the event that broker–dealers with whom they transact business encounter financial difficulties and are unable to satisfy their obligations to their public customers, the court declining to appoint a trustee and trustee's counsel nominated by the SIPC, on the ground that the trustee was a member of a law firm which represented a major creditor of the debtor, and the counsel appointed was the same law firm.

Legislative history of SIPA, as well as language of *15 U.S.C.A. § 78fff*(c)(2)(A)(ii), makes it plain that SIPA is designed to protect customers who have either cash, or securities, or both, in custody of broker–dealer firms. *Re Atkeison (MD Tenn) 446 F Supp 844.*

One objective of § 60(e) of Bankruptcy Act *(11 U.S.C.A. § 96*(e)) was to eliminate, in bankruptcy proceedings, conflict in rules and to create rules which would be uniform throughout nation; interest in uniformity of treatment of insolvent brokerage houses was furthered through Securities Investor Protection Act which, in *15 U.S.C.A. § 78fff,* adopts, to large degree, provisions of § 60(e) and makes them applicable to brokerage house liquidation proceedings under *SIPA. Securities & Exchange Com. v First Secur. Co. (CA7 Ill) 507 F2d 417.*

Securities Investor Protection Act (SIPA) provides relief to certain classes of a failed broker/dealer's customers. Securities Investor Protection Act of 1970, §§ 1(a) et seq., *15 U.S.C.A. §§ 78aaa* et seq. *In re John Dawson & Associates, Inc., 289 B.R. 654 (Bankr. N.D. Ill. 2003).*

Purposes of Securities Investor Protection Act were to protect against individual hardship caused to customers of brokerage houses by broker failures, to restore investor confidence, and to upgrade financial responsibility required of registered brokers and dealers. *Securities & Exchange Com. v White & Co. (CA8) 546 F2d 789.*

In *Lohf v Casey (1972, CA10 Colo) 466 F2d 618,* the court stated that the SIPA was designed to afford protection to the customers of broker–dealers who fell into financial difficulty and that the SIPC was created to implement the

protection plan.

Congress passed the Securities Investor Protection Act (SIPA) to protect public investors against financial losses arising from insolvency of registered brokers and dealers. Securities Investor Protection Act of 1970, §§ 1(a) et seq., as amended, *15 U.S.C.A. §§ 78aaa* et seq. *In re Primeline Securities Corp., 295 F.3d 1100, 39 Bankr. Ct. Dec. (CRR) 211 (10th Cir. 2002).*

Securities Investor Protection Act was passed in order to afford some protection to public customers against financial loss as consequence of bankruptcy of their stockbrokers. *Securities Investor Protection Corp. v Associated Underwriters Corp. (DC Utah) 423 F Supp 168.*

Announcement and interpretation of rule relating to allocaton of regulatory responsibility among self–regulatory organizations having members in common pursuant to 9(c) of Securities Investor Protection Act *(15 U.S.C.A. §§ 78iii*(d)). Securities Exchange Act of 1934, Release No. 12352, SEC Docket Vol 9, p 450.

[*3.] 5 Exemptions

Massachusetts Financial Services, Inc. was not member of Securities Investor Protection Corp. and was not liable for sum which it had paid to SIPC as mandatory assessment for two calendar years; corporation was exempt from membership in SIPC since all of corporation's activity as broker–dealer was statutorily exempted. *Massachusetts Financial Services, Inc. v Securities Investor Protection Corp. (CA1 Mass) 545 F2d 754.*

[*4] Constitutionality

In the following cases, the SIPA, or particular constructions of its provisions, were held not to be unconstitutional.

Also, see *Securities & Exchange Com. v Milner (1973, CA1 Mass) 474 F2d 162,* an action brought by securities salesmen for commissions and, by one of them, for losses as a customer and general creditor of a registered broker–dealer whose business was being liquidated by a trustee appointed under the provisions of the SIPA, both of the salesmen having appealed from an order of the District Court directing the trustee to make distribution in accordance with his plan, where the court, while stating that it declined to consider an attack upon the alleged unconstitutionality of the Act since such attack had not been made in the District Court, recognized that well before the enactment of the SIPA, securities customers were recognized as retaining a special interest in customer property, and that both earlier practice and valid social and economic aims would seem to provide a rational basis for the "single and separate fund" provisions of the SIPA. (From the face of the court's opinion, the court's remarks appear to have been made in response to a contention to the effect that the "single and separate fund" provisions were so irrational as to violate due process.)

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144,* the court held that due process considerations do not require that an opportunity for a hearing be afforded at the time of the SIPC's determination of the need for petitioning the District Court to invoke the Act, the court explaining that such initial determination, in itself, has no binding legal consequences and does not deprive the broker–dealer of property. However, the court held that due process considerations demand that the Act be interpreted to require that the District Court, under § 5(b) of the SIPA *(15 U.S.C.A. § 78eee*(b)), make a de novo determination that the protection of the Act is necessary, the court stating that it is not sufficient that some lesser process take place merely involving judicial review of the initial administrative determination of the SIPC. The court stated that due process requires the opportunity for a hearing appropriate to the nature of the case, adding that the factual issues involved in the District Court's determination under § 5(b) are so complex that an opportunity to confront and cross–examine adverse witnesses will almost always be required.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1973, CA2 NY) 481 F2d 401,* cert den *414 US 1092, 38 L Ed 2d 549, 94 S Ct 722,* the court after rejecting arguments that the SIPA itself permitted payment of attorneys' fees incurred in defending an action brought against a broker–dealer by the SIPC, payment to be made from the remaining estate of the dealer, also rejected arguments that such a construction of the Act would impose upon respondents to SIPC liquidation applications the unconstitutional deprivation of the assistance of counsel. Appellants who had served as counsel to a broker–dealer in such a proceeding pointed out that the SEC and the SIPC frequently act in tandem to tie up a firm's assets pending judicial determination of the application for a trusteeship and liquidation, and further argued that counsel would not undertake a defense without assurance of subsequent payment. The court answered that the defendants in the instant case suffered no deprivation of legal services and that the same willingness of attorneys to represent a debtor resisting involuntary proceedings under the Bankruptcy Act was a frequent phenomenon. The court added that it did not understand the law to be that, as a general matter, the Constitution requires the appointment of counsel for litigants in civil cases, and

that it had long been held that legal services in resisting a bankruptcy petition were not compensable under that Act, such construction of the law not having been seriously doubted from a constitutional point of view. Moreover, concluded the court, if the Constitution does not require exemption from a filing fee for an indigent who seeks to take advantage of the bankruptcy laws, it surely does not require that a brokerage firm resisting an application under SIPC be entitled to have its attorneys paid out of the estate. (For a discussion of the statutory arguments made in this case concerning the allowance of attorneys' fees, see § 24[a] , infra.)

In *Securities & Exchange Com. v Albert & Maguire Secur. Co. (1974, DC Pa) 378 F Supp 906,* where margin customers of a broker in liquidation under the SIPA sought, through payment of the amounts owing on securities held by the broker at the time of the initiation of the liquidation proceedings, to obtain the proceeds from the sale of those securities by the trustee, the court rejected the contention of the customers that the Act was unconstitutional, the court stating that the purpose of the Act was primarily to protect the rights of customers against inequities which had been shown to exist, and that the Act met the guarantee of due process under the Fifth Amendment since it was not an unreasonable, arbitrary, or capricious means of accomplishing the object sought to be obtained.

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In the following case, subsequently reversed without opinion, the court held that the requirement that the District Court appoint the persons specified by the SIPC to be trustee and attorney for the trustee *(15 U.S.C.A. § 78eee*(b)(3)) was unconstitutional.

In *Securities & Exchange Com. v Oxford Secur. Ltd. (1973, DC NY) 354 F Supp 301,* revd without op (CA2 NY) *486 F2d 1396,* the court, denying the SIPC's application for the appointment of a specified trustee and attorney for the trustee, stated that on its face, the statutory provision purporting to require such appointment left no room for judicial discretion and did not call for the performance of a judicial act, but merely mandated a purely ministerial duty which was outside the judicial powers vested in the court by the Constitution; that this statutory provision offended the separation of powers of the legislative, judicial, and executive branches of the government; and that the court therefore could not constitutionally nor conscientiously comply with the requirement of the provision.

[*5] Prospective application

In the following decisions involving applications for the protection afforded by the SIPA, the courts determined that it was the intent of Congress that the provisions of the SIPA be applied prospectively from the date of its enactment, so that the Act would extend its protection only to customers of those businesses that were actually in business in the usual sense as "brokers or dealers" as of that date, and that the Act did not extend retroactively to those brokers or dealers that had ceased doing business at the effective date of the legislation.

Where customers of a securities brokerage firm sought the protection of the SIPA as a result of alleged wrongful acts of the firm and its directors, the court in *Bohart–McCaslin Ventures, Inc. v Midwestern Secur. Corp. (1973, DC Tex) 352 F Supp 937,* held that because the alleged activities had occurred prior to the effective date of the Act, the Act did not apply to such activities. The court stated that the SIPA was not intended to provide protection to customers of securities companies which were in serious difficulty prior to the effective date of the Act. The court pointed out that although the firm continued to be registered as a broker–dealer with the Securities and Exchange Commission, it had ceased doing business in that capacity at the time the SEC had obtained an injunction enjoining it from further violations of the securities acts, approximately a year prior to the effective date of the SIPA. The court stated that the question was not whether Congress intended the statute to be retroactive, but rather which firms, in light of their financial status, Congress intended to be covered by the Act. Thus, concluded the court, the customers bringing the action must be excluded from the protection of the Act even if Congress intended that the SIPC might draw upon facts relating to a broker's condition existing prior to the effective date of the Act when making a determination as to the broker's insolvency or inability to carry on his business, as required under the Act.

The court held that the SIPA was not to be applied retroactively, but that where an insolvent broker had engaged in substantial business, having handled in excess of 110 transactions, after the effective date of the Act, the Act's application to that broker did not constitute retroactive application, in *Securities & Exchange Com. v Guaranty Bond & Secur. Corp. (1974, CA6 Tenn) 496 F2d 145,* cert gr (US) *42 L Ed 2d 138, 95 S Ct 172,* the court reversing the trial court's decision to the contrary and remanding. Upon determining that the broker had operated for a substantial period of time while in violation of the SEC's net capital rule (for a discussion of the net capital rule, see the annotation at *19 ALR Fed 9),* the Commission had successfully applied for the appointment of a receiver to take charge of the assets of the broker, subject

to further orders of the court. Noting that the SEC had brought the action after the effective date of the SIPA, the court stated that the Commission's filing of that action did not prevent the broker from conducting normal business after the effective date of the Act, and held that in view of the transactions conducted subsequent to the effective date, the broker, though financially weak, was in fact a broker or dealer as of the effective date of the Act, and that the provisions of the Act therefore applied. The court also stated that it was the intention of Congress that losses which had been experienced by the industry prior to the effective date of the Act were to be regarded as the industry's responsibility.

In *Lohf v Casey (1972, CA10 Colo) 466 F2d 618,* an action involving an application by a trustee of a bankrupt brokerage firm seeking the protection of the SIPA for the customers of the firm, the Court of Appeals upheld the trial court's determination that the SIPA was inapplicable to the firm, because it had been adjudicated bankrupt prior to the enactment of the SIPA. The trustee asserted that notwithstanding that the bankruptcy proceedings predated the effective date of the Act, the bankrupt brokerage was nevertheless a member of the SIPC because its registration as a broker–dealer with the SEC had not been withdrawn or terminated. The court stated, however, that at the effective date of the Act, the brokerage was not conducting its business as a broker or dealer and could not be considered a broker or dealer, whether registered or not, even though its automatic membership in the SIPC may have come about. The court stated that the legislative history made it clear that the Act was to be prospective from the date of its enactment, and that only those firms or persons which were actually in business in the usual sense at that critical date were "brokers or dealers" under the Act, the court concluding that the Act did not apply to firms which had failed prior to that date.

[*6] Standing

The decisions are not uniform as to whether private individuals have standing to bring an action to compel the SIPC to invoke the provisions of the SIPA.

In the following decision, the court held that private individuals do not have standing to invoke the Act's protection since, under *15 U.S.C.A. § 78ggg*(b), only the SEC can seek to compel SIPC to take action under the Act.

In an action brought by two corporations, various officers thereof, and a private individual against a brokerage house, its directors, and others, and in which action the plaintiffs sought the protection of the SIPA as a result of the alleged wrongful acts of the brokerage house and its directors, the court, in *Bohart–McCaslin Ventures, Inc. v Midwestern Secur. Corp. (1973, DC Tex) 352 F Supp 937,* held that the plaintiffs had no standing to bring suit against any of the defendants under the SIPA. The court pointed out that under § 7(b) of the SIPA *(15 U.S.C.A. § 78ggg*(b)), in the event of the refusal of the SIPC to commit its funds or otherwise to act for the protection of customers of any member of the SIPC, the SEC may apply to a District Court for an order requiring the SIPC to discharge its obligations under the Act, but that the court interpreted that provision to mean that only the SEC could bring such a suit. The court stated that the SIPC's powers are discretionary except when it is required to act pursuant to a court action initiated by the SEC. The court added that § 7(b) provides the only means by which a court may order the SIPC to provide protection under the Act when the SIPC has not determined the need for such protection, so that, in essence, the private individuals did not have standing to maintain the instant action.

On the other hand, in the following case, the court held that since the language of *15 U.S.C.A. § 78ggg*(b), authorizing the SEC to bring an action to compel the SIPA to invoke the Act, was not exclusive, and since *15 U.S.C.A. § 78ccc*(b)(1) generally provides for suits against the SIPC, customers of a broker or dealer, or a receiver of a broker–dealer acting on behalf of the customers, had standing to seek enforcement of the act by the SIPC.

A provision of the Securities Investor Protection Act *(15 U.S.C.A. § 78eee*(d)), under which the Securities Investor Protection Corporation is deemed to be a party in interest as to all matters arising in a liquidation proceeding and is deemed to have intervened with respect to all such matters, does not—either alone or with a provision of the Racketeer Influenced and Corrupt Organizations Act *(18 U.S.C.A. § 1964*(c)), which provides that any person injured in his business or property by reason of a violation of RICO may sue therefor in any appropriate United States District Court—give SIPC a right to sue an alleged conspirator in a stock manipulation scheme to recover funds advanced by SIPC, pursuant to *15 U.S.C.A. § 78fff–3*(b)(2), to trustees for administering liquidation proceedings with respect to broker–dealers that were allegedly disabled by the scheme from meeting obligations to customers, given that § 78eee(d) says nothing about the conditions necessary for SIPC's recovery as a plaintiff. *Holmes v Securities Investor Protection Corp. (1992, US) 117 L Ed 2d 532, 112 S Ct 1311, 92 CDOS 2460, 92 Daily Journal DAR 4030, CCH Fed Secur L Rep P 96555,* remanded, on remand (CA9) *92 CDOS 4264, 92* Daily Journal DAR 6741.

Customers of failing broker–dealers do not have implied right of action under Securities Investor Protection Act to

compel Securities Investor Protection Corporation to exercise its statutory authority for their benefit, since even though Act does not expressly preclude private cause of action, and even though brokers' customers are intended beneficiaries of Act, (1) § 7(b) of Act *(15 U.S.C.A. § 78ggg*(b)) authorizes suits by Securities and Exchange Commission to compel Corporation to proceed under Act, (2) there is no extrinsic evidence that Congress also intended to allow private action, and (3) private right of action would not be consistent with structure or purpose of Act. *Securities Investor Protection Corp. v Barbour 421 US 412, 44 L ED 2d 263, 95 S Ct 1733.*

Trustee for insolvent broker–dealer, appointed under Securities Investor Protection Act, has standing to bring action against registered national securities exchange based upon its failure to enforce its rules and regulations where such failure damaged estate. *Collins v PBW Stock Exchange, Inc. (DC Pa) 408 F Supp 1344.*

The court held that a receiver, appointed at the request of the SEC, for an insolvent broker had standing to bring an action to invoke the provisions of the SIPA, in *Securities & Exchange Com. v Guaranty Bond & Secur. Corp. (1974, CA6 Tenn) 496 F2d 145,* cert gr (US) *42 L Ed 2d 138, 95 S Ct 172.* The SEC had obtained the appointment of the receiver upon its determination that the broker had operated for a substantial period of time while in violation of the Commission's net capital rule (for a discussion of the net capital rule, see the annotation at *19 ALR Fed 9),* whereupon the receiver filed a petition for an order directed to the SEC and the SIPC requiring each of them to show cause why the SIPC should not be required to intervene in the action and afford to the customers of the broker the benefits of the Act. The court rejected the arguments of the SEC and the SIPC that absence of express language providing for an enforcement action by customers of a security company, or their representatives, prohibited the receiver from bringing the action. The court stated that the lack of express language of exclusivity in provisions providing for an enforcement action by the SEC, coupled with a general provision allowing for suits against the SIPC, a provision contained in *15 U.S.C.A. § 78ccc*(b)(1), evidenced an intent on the part of Congress to permit customers or their representatives to bring actions under the Act. Pointing out that the receiver was a representative of the customers of the broker, the court held that the receiver was a proper party to seek to have the SIPC meet its obligations to the customers under the broad purposes of the Act.

**** Caution:

To extent that any cases discussed in § 6 of *23 ALR Fed 157* are inconsistent with Supreme Court's decision in *Securities Investor Protection Corp. v Barbour, 421 US 412, 44 L ED 2d 263, 95 S Ct 1733,* infra, it would appear that such cases are no longer of precedential value.

As bailee of customer property, Securities Investor Protection Corporation (SIPC) had standing to bring claims for bank's alleged lack of care and negligence in handling accounts that were used by financial services company that SIPC was appointed to liquidate, and company's principal officer, in embezzling customers' funds, but only to the extent that customers had not been paid. *In re Meridian Asset Management, Inc., 296 B.R. 243 (Bankr. N.D. Fla. 2003).*

[*III] Incorporation of Bankruptcy Act

[*7] Generally

The following decisions have applied the provisions of § 6 of the SIPA *(15 U.S.C.A. § 78fff*(c)) to the effect that except as inconsistent with the SIPA, provisions of the Bankruptcy Act are applicable to liquidations under the SIPA.

The court noted that certain provisions of the Bankruptcy Act are, by express provision of the SIPA, applicable to SIPC liquidations, in *Securities & Exchange Com. v Alan F. Hughes, Inc. (1973, CA2 NY) 481 F2d 401,* cert den *414 US 1092, 38 L Ed 2d 549, 94 S Ct 722,* where the court held, on the basis of the law under the Bankruptcy Act, that attorneys for a broker–dealer were not entitled to their fees as a matter of first priority from the estate of the broker–dealer, or from SIPC funds, or from both, for their services in resisting an application by the SIPC for appointment of a trustee and liquidation of the broker–dealer. The attorneys argued that in the context of an SIPA liquidation, they should be allowed such compensation despite authority that resisting a bankruptcy application did not so aid the administration of the estate as to warrant a first priority claim under § 64a of the Bankruptcy Act *(11 U.S.C.A. § 104*(a)), which provides for the payment of reasonable attorneys' fees in bankruptcy cases. The attorneys based their argument on the fact that, in a liquidation under the SIPA, the proceeding may commence even though the broker–dealer may be solvent, and unlike a straight bankruptcy proceeding, allowance of such attorneys' fees would not affect the moneys going to the broker–dealer's customers. In rejecting those arguments, the court pointed out that a liquidation under the SIPA cannot be ordered unless the court finds that the broker–dealer has failed or is in danger of failing to meet its obligations to its customers, and that while allowing fees to attorneys for defendants in SIPA proceedings would not reduce funds available for most

broker–dealer customers, it still did not follow that when incorporating the Bankruptcy Act provisions into the SIPA, Congress intended to exclude well–settled judicial interpretations of the provisions so incorporated.

In affirming the fee awarded a trustee and his counsel for services rendered in an SIPA liquidation, the court in Securities Investor Protection Corp. v Charisma Securities Corp. (1974, CA2 NY) *CCH Fed Secur L Rep P 94878,* held that § 241 of the Bankruptcy Act *(11 U.S.C.A. § 641),* which requires a judge to scrutinize reasonableness of fee awards in Chapter X proceedings, is incorporated in the SIPA through the operation of § 6(c)(1) of the Act *(15 U.S.C.A. § 78fff*(c)(1)). Noting that § 6(c)(1) incorporates those provisions of Chapter X which are not inconsistent with the SIPA, the court stated that a provision is "inconsistent" with the SIPA if it conflicts with an explicit provision of the Act, or if its application would substantially impede the fair and effective operation of the SIPA without providing significant countervailing benefits. The court added that a provision does not become "inconsistent" merely because it is not absolutely necessary for the operation of the Act, the court commenting that a district judge would therefore not be justified in disregarding, as one relevant factor, the need for sensible and economical administration because the SIPC was paying the fee.

In proceedings under Securities Investor Protection Act, court may make general reference of proceedings to bankruptcy referee since § 6(c)(1) of Act *(15 U.S.C.A. § 78fff*(c)(1)) states that proceedings under Act shall be conducted in accordance with certain provisions of Bankruptcy Act, including § 22 of that Act which provides for such general references. *Exchange Nat. Bank v Wyatt (CA2 NY) 517 F2d 453.*

In *Securities Investor Protection Corp. v Charisma Secur. Corp. (1972, DC NY) 352 F Supp 302,* an action involving an application for an interim fee allowance to a trustee and his counsel for services rendered in the liquidation of a brokerage business pursuant to the provisions of the SIPA, the court, in commenting upon the applicability of the Bankruptcy Act to SIPA proceedings, stated that the SIPA requires that liquidation proceedings be conducted in accordance with, and as though they were being proceeded with under, Chapter X of the Bankruptcy Act. The court continued that in equating an SIPC liquidation with a Chapter X reorganization, the purpose was to adequately serve the public interest in such matters at a level somewhat different from straight bankruptcy proceedings, the primary criterion being not rigid economy as in straight bankruptcy.

As also applying provisions of the Bankruptcy Act to liquidation proceedings under the SIPA, see the following cases: *Securities & Exchange Com. v Kenneth Bove & Co. (1973, DC NY) 353 F Supp 496* , infra § 14 ; *Re Buttonwood Secur., Inc. (1972, DC Cal) 349 F Supp 273,* infra § 15 .

Reconsideration of claims under Securities Investor Protection Act by court is governed by Rule 307 of Rules of Bankruptcy Procedure; motion to reconsider is addressed to discretion of court; court is to apply equitable doctrines of laches and estoppel in deciding whether to reconsider claim. *Securities & Exchange Com. v E.P. Seggos & Co. (DC NY) 416 F Supp 280.*

Clear intent of Securities Investor Protection Act *(15 U.S.C.A. §§ 78aaa* et seq.) is to make § 241 of Bankruptcy Act applicable to fee allowances in brokerage liquidations. *Securities & Exchange Com. v Kenneth Bove & Co. (SD NY) 451 F Supp 355.*

Section 243 of Chapter X of Bankruptcy Act does not relate to conduct of administration or liquidation procedures to be followed, but serves to redress balance of power between insiders and outsiders during corporate reorganization; under Securities Investor Protection Act, insiders are replaced by neutral trustee appointed by court at request of Securities Investor Protection Corporation and thus goal of equalizing power of large and small creditors has been met by means other than those embodied in § 243; accordingly, § 243 of Chapter X has not been incorporated in SIPA by § 6(c) of that Act *(15 U.S.C.A. § 78fff*(c)). *Securities & Exchange Com. v Aberdeen Secur. Co. (CA3) 526 F2d 603.*

In awarding fees to an attorney by reason of his successful representation of a client regarding his claim under the SIPA, the court, in *Securities & Exchange Com. v Aberdeen Secur. Co. (1974, DC Del) 381 F Supp 614,* pointed out that under the SIPA, liquidation proceedings were to be conducted in accordance with, and as though they were being proceeded with under, Chapter X of the Bankruptcy Act. The court said that § 243 of Chapter X *(11 U.S.C.A. § 643),* which permits the court to award compensation to an attorney for services which were beneficial in the administration of the estate, was applicable to the case, the court concluding that since the attorney's services had brought about recognition of lawful claims which otherwise would not have been paid, the attorney's services were of benefit to the estate within the meaning of the Bankruptcy Act, as incorporated in the SIPA.

In *Securities & Exchange Com. v Wick (1973, DC Ill) 360 F Supp 312,* an action involving the question whether an

individual who operates the business of a broker–dealer as a sole proprietorship subjects not only his business assets, but also his personal assets, to liquidation under the SIPA, the court recognized the express applicability of certain provisions of the Bankruptcy Act to the SIPA, but stated that it was clear from the language as well as from the history and purpose of the SIPA, that the SIPA did not supersede the provisions of the Bankruptcy Act which had governed the manner and method by which an insolvent broker–dealer's business was liquidated prior to the enactment of the SIPA. Citing legislative intent contrary to the argument that the SIPA was intended to supplant the Bankruptcy Act in broker–dealer liquidation proceedings, the court found that the effect of the SIPA upon the Bankruptcy Act is strictly limited, and that only those sections of the Bankruptcy Act which would frustrate the ability of the SIPC to protect the customer's funds, in a manner analogous to the similar Federal Savings and Loan Insurance Corporation, are superseded by the sections of the SIPA which are more consistent with this legislative purpose than are comparable sections of the Bankruptcy Act. Consequently, concluded the court, once a broker–dealer falls below the solvency standards established by the Securities and Exchange Commission, the subsequent liquidation of his assets for the benefit of creditors proceeds under the Bankruptcy Act.

Procedural rights accorded stockholders by § 206 of Chapter X of Bankruptcy Act *(11 U.S.C.A. § 606)* are inconsistent with provisions of SIPA, and therefore not applicable under *15 U.S.C.A. § 78fff* (c)(1), since formulation of any plan of reorganization in SIPA proceeding is expressly prohibited by § 78fff(c). *Securities & Exchange Com. v Securities Northwest, Inc. (CA9) 573 F2d 622.*

[*8] Summary jurisdiction

In the following case, the court held that although Chapter X of the Bankruptcy Act generally applies in an SIPA liquidation proceeding, and although the federal courts generally have summary jurisdiction in Chapter X proceedings, summary jurisdiction is not present in an SIPA liquidation proceeding, just as it is not present in a Chapter X proceeding where liquidation is ordered.

Stating that although the provisions of Chapter X of the Bankruptcy Act apply to liquidation proceedings under the SIPA, and that although Federal District Courts generally have summary jurisdiction in Chapter X proceedings, the court, in Securities & Exchange Com. v Morgan Kennedy & Co. (1974, DC NY) *CCH Fed Secur L Rep P 94568,* held that summary jurisdiction over parties asserting claims to property sought to be recovered by the trustee in an SIPA liquidation does not exist. The court said that although Congress gave considerably more latitude to an SIPA court than to an ordinary bankruptcy court, by granting to the former the broader powers of a Chapter X court, Congress intended the SIPA to be a statute with the dominant purpose of liquidation and not reorganization. The court stated that § 23 of the Bankruptcy Act *(11 U.S.C.A. § 46),* which requires a bankruptcy trustee to proceed by plenary suit to resolve disputes with parties adversely holding property claimed by the trustee on behalf of the estate, generally does not apply to Chapter X proceedings, but, pursuant to § 102 of the Bankruptcy Act *(11 U.S.C.A. § 502),* § 23 does apply where a bankruptcy liquidation is ordered. Concluding that Congress intended that an SIPA proceeding be governed by rules applicable to a liquidating reorganization under Chapter X, the court stated that the adverse claimants had successfully challenged the court's summary jurisdiction and that the trustee must litigate its dispute in a plenary hearing.

[*IV] Determination of need for customer protection

[*9] Generally

The following case supports the view that in a District Court's determination that the customers of a broker–dealer are in need of the protection of the SIPA, it is necessary that the District Court find that only one of the five conditions enumerated in *15 U.S.C.A. § 78eee*(b)(1) exists, and that the District Court also find, under *15 U.S.C.A. § 78eee*(a)(2), that the broker–dealer has failed, or is in danger of failing, to meet its obligations.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144,* an action in which a broker–dealer appealed from an order of the District Court appointing a trustee pursuant to the provisions of SIPA, the Court of Appeals made it clear that the appointment of a trustee is sustainable on the basis of a finding of the existence of only one of the five conditions enumerated under § 5(b)(1)(A) of the Act *(15 U.S.C.A. § 78eee*(b)(1)(A)), but that in addition to finding that one of these five conditions exists, the District Court must find, under § 5(a)(2) of the Act *(15 U.S.C.A. § 78eee*(a)(2)), that the broker–dealer was in danger of failing to meet its obligations, the court emphasizing that the SIPC, in its petition pursuant to the SIPA, need show only that there is a danger that the broker–dealer will fail to meet its obligations, but not that it has actually done so.

Since Securities Investor Protection Act was enacted under commerce power, and not under bankruptcy powers,

District Court cannot delegate to bankruptcy referee determination, under § 5 of Act, of whether provisions of Act should be imposed, but after that determination has been made, it is not unconstitutional for court to make general reference to bankruptcy referee. *Exchange Nat. Bank v Wyatt (CA2 NY) 517 F2d 453.*

When a claimant deposits funds with brokerage for investment, the Securities Investor Protection Act (SIPA) provides protection, even if claimant does not identify specific securities for broker to purchase. Securities Investor Protection Act of 1970, § 16(2, 14), as amended, *15 U.S.C.A. § 78lll*(2, 14). *In re Primeline Securities Corp., 295 F.3d 1100, 39 Bankr. Ct. Dec. (CRR) 211 (10th Cir. 2002).*

[*10] De novo determination by court

[*10a] Necessity

In the following case, it was held that the District Court, under *15 U.S.C.A. § 78eee*(b)(1)(A), must make its own de novo determination of the need for customer protection under the SIPA, and that due process does not require an opportunity for a hearing at the time of the initial SIPC determination.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144*, an action in which a broker–dealer challenged the appointment of a trustee pursuant to the provisions of the SIPA, the court held that following a determination by the SIPC that a broker–dealer has failed, or is in danger of failing, to meet its obligations to its customers, so that application of the Act is necessary, due process requires that the District Court make its own de novo determination that the protection of the Act is necessary. The court stated that it is not sufficient that some lesser process take place, merely involving judicial review of the initial administrative determination. The court recognized that some authority arguably suggests that a de novo judicial proceeding is not necessary to cure the absence of an initial administrative hearing, but stated that it was clear that one of the minima of due process is the opportunity for hearing appropriate to the nature of the case, and that a determination as to whether a member of the SIPC has failed or is in danger of failing to meet its obligations to its customers involves the resolution of difficult and complex factual issues, so that an opportunity to confront and cross–examine adverse witnesses is almost always required. The court further stated that it was unaware of any exigencies or practical problems of administration that might justify any less stringent view of what must be done in the District Court proceeding under the Act. In view of this, explained the court, due process does not require that an opportunity for a hearing be afforded at the time the SIPC makes its initial determination that one of its members has failed or is in danger of failing to meet its obligations to its customers, and that there exists one or more of the conditions specified in § 5(b)(1)(A) of the Act *(15 U.S.C.A. § 78eee*(b)(1)(A)). That initial determination, in and of itself, explained the court, has no binding legal consequences and deprives no broker–dealer of property; rather, that determination is merely a preliminary step in the process by which the SIPC decides to apply to a District Court for a decree adjudicating that the customers of a member firm are in need of the protection provided by SIPA. The court declared that under the SIPA, due process is satisfied so long as the District Court, after providing the broker–dealer with an opportunity to be heard, makes its own determination that the broker–dealer has failed or is in danger of failing to meet its obligations to its customers.

[*10b] Adequacy

Under the circumstances of the following case, it was held that the de novo hearing that had taken place in the District Court, wherein it had been determined that the customers of a broker–dealer were in need of the protection of the SIPA, had satisfied the requirements of the SIPA.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144*, an action in which a broker–dealer appealed from a District Court order appointing a trustee pursuant to the application of the SIPC, and in which the broker–dealer, challenging the sufficiency of the hearing held in the District Court, argued that the District Court had not realized that it was obligated to make its own findings with respect to the validity of the SIPC's determination that the broker–dealer was in danger of failing to meet its obligations to its customers and that the customers were in need of the protection of SIPA, the Court of Appeals concluded that this claim was not supported by the record. On the contrary, found the Court of Appeals, counsel for SIPC conceded at the District Court hearing that the District Court should make its own findings about the ability of the broker–dealer to meet its obligations to its customers. The Court of Appeals stated that the fact that the District Court judge accepted this interpretation and recognized his responsibility to make such a determination was shown by his permitting defense counsel to argue that the evidence failed to show any danger that the dealer would fail to meet its obligations to its customers. Furthermore, stated the Court of Appeals, the District Court had specifically found that the dealer was in danger of failing to meet its obligations to its customers, and it

was unlikely that the District Court would have made the finding unless it had believed that this was a prerequisite to its adjudicating the customers to be in need of protection provided by SIPA. Also, the Court of Appeals held that the hearing before the District Court provided the broker–dealer with ample opportunity to present evidence, if it had wanted to do so, relating to its ability to meet its obligations to its customers. The Court of Appeals further pointed out that in appointing the trustee under the SIPA, the court did not rely solely upon oral statements made during the hearing, but also relied upon all the evidence which had been accumulating from the time the SEC initially commenced its action, the Court of Appeals concluding that the dealer was accorded due process in the hearings which the court had conducted.

[*11] Adequacy of findings necessary for determination of customers' need for protection

[*11a] Finding that broker was in danger of failing to meet obligations

Under the circumstances of the following case, the court found that the record amply supported the finding that the broker–dealer had been in danger of failing to meet its obligations to its customers, which finding, under *15 U.S.C.A. § 78eee*(a)(2), was necessary to the determination that the customers of the broker–dealer were in need of the protection of the SIPA.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144*, an action in which a broker–dealer appealed from an order of a District Court appointing a trustee pursuant to the provisions of the SIPA, the Court of Appeals held that the finding that the broker–dealer was in danger of failing to meet its obligations to its customers was clearly supported by the record. The Court of Appeals pointed out, for instance, that in the case of one customer who gave the dealer $100,000 for the purchase of securities, the principal stockholder of the broker–dealer corporation diverted the money to its own personal use for several months; that when the securities were ultimately purchased for the account of the customer, some of them were unlawfully hypothecated; and that as of the time of the special fiscal agent's report, the customer had still been unable to obtain possession of some of its securities, because they had been pledged as security for unpaid loans of the dealer. The report of the fiscal agent, pointed out the Court of Appeals, contained information that the broker–dealer had also unlawfully hypothecated the securities of other customers, and that it had engaged in practices which reflected upon its integrity as a broker. Finally, the Court of Appeals stated, the report of the special fiscal agent indicated that the records of the broker–dealer were too misleading and inaccurate to be of any value in determining whether the dealer had violated the federal securities laws. The Court of Appeals concluded that in view of the fact that the SIPC had only to show that there was a danger that the dealer would fail to meet its obligations, not that it had actually done so, any contention that the SIPC had failed to make the requisite showing was utterly without merit.

[*11b] Finding of existence of one or more of conditions specified in *15 U.S.C.A. § 78eee*(b)(1)(A)

In the following case, it was held that the district court properly had found the existence of two of the five conditions specified in *15 U.S.C.A. § 78eee*(b)(1)(A), it being noted that one of these five conditions had to be satisfied to justify a determination that the customers of the broker–dealer were in need of the protection of the SIPA.

In *Securities & Exchange Com. v Alan F. Hughes, Inc. (1972, CA2 NY) 461 F2d 974, 23 ALR Fed 144*, where a broker–dealer appealed from the District Court's appointment of a trustee under the SIPA, the Court of Appeals, in affirming that appointment, held that the District Court correctly found that two of the five conditions set forth in § 5(d)(1)(A) of the SIPA *(15 U.S.C.A. § 78eee*(b)(1)(A)) existed. Specifically, the Court of Appeals pointed out that the District Court properly had found that the dealer was unable to make such computations as may have been necessary to establish compliance with financial responsibility or hypothecation rules or regulations. The Court of Appeals stated that such finding was supported by a report of the special fiscal agent which concluded that the defendant's books and records were so unreliable, inaccurate, incomplete, and misleading that they were unusable, and that this finding was corroborated by an accounting firm whom the special fiscal agent had hired to audit the books. The Court of Appeals also stated that the District Court had correctly found that the broker–dealer was the subject of a proceeding, pending in a court, in which a receiver for such broker–dealer had been appointed, the Court of Appeals pointing out that the District Court itself had appointed a receiver for the broker–dealer.

[*V] Appointment of trustee and trustee's counsel

[*12] Requirement that trustee and counsel be disinterested

Under § 5(b)(3) of the SIPA *(15 U.S.C.A. § 78eee*(b)(3)), a trustee and the attorney for a trustee may be appointed only if they are "disinterested, " within the meaning of § 158 of the Bankruptcy Act *(11 U.S.C.A. § 78o*(c)(3)). This

requirement of disinterestedness was applied in the following cases.

The court recognized that a trustee and trustee's counsel appointed under the SIPA must be disinterested, in Handelman v Weiss (1973, DC NY) *CCH Fed Secur L Rep P 94214*, an action to recover for alleged violations of the antifraud provisions of the federal securities laws brought by customers against a brokerage firm, and an action where the court, upon defense motion, disqualified one law firm from representing a customer in the action and from having any connection with the litigation because one of the partners of the law firm had been an assistant to the counsel for the trustee appointed under the SIPA to liquidate the defendant brokerage house. In discussing the requirements of a trustee and his counsel under the SIPA, the court noted that the person selected as trustee to conduct a liquidation pursuant to the provisions of the Act must be "disinterested," which, explained the court, means that he cannot be an attorney for the debtor or have any interest materially adverse to that of the creditors or the stockholders of the debtor. The court noted that while the duties of the attorney for the trustee are not specifically spelled out in the SIPA, it seemed clear that his obligation was to assist the trustee in the performance of his task.

Declining to appoint the trustee and trustee's counsel nominated by the SIPC, the court, in *Securities & Exchange Com. v Schreiber Bosse & Co. (1973, DC Ohio) 368 F Supp 24*, pointed out that the trustee nominated was a member of a law firm which acted as outside counsel for a major creditor of the debtor, and that the counsel nominated was the same law firm. Emphasizing that the SIPA required that the trustee and his attorney be "disinterested," within the meaning of that term as defined in Chapter X of the Bankruptcy Act, the court stated that the standard of disinterestedness must be strictly applied, and that the trustee must be divested of any scintilla of personal interest which might be reflected in his decision concerning estate matters. The court pointed out that in addition to the fact that the law firm acted as legal counsel for the creditor, whose claim was for approximately 18 percent of the liabilities of the debtor, members of the law firm also were on the creditor's board of directors. The court stated that the trustee and his attorney, if appointed, would be placed in a posture of potential conflict with respect to the claim of the creditor, in that, on the one hand, they were charged with the duty of recommending the allowance of the creditor's claim and of advising as to compromise or objecting to claims, and on the other hand, the law firm would be concerned with remaining in the good graces of its client. The court therefore directed the SIPC to select a different trustee and attorney.

[*VI] Claims against and administration of estate

[*A] In general

[*13] Includibility in estate of securities received after filing

In the following case, the court held that securities received after the filing date by a trustee in an SIPA liquidation were not a part of the estate, since title did not pass to the debtor prior to the initiation of the liquidation.

It was held in Securities & Exchange Com. v John E. Samuel & Co. (1973, DC NY) *CCH Fed Secur L Rep P 93720*, that securities received by the trustee, pursuant to contracts entered into by the broker in liquidation prior to the filing date, were not part of the estate and were required to be returned to the senders, even though they had been indorsed to the broker and mailed prior to the filing date. Pointing out that the date of commencement of liquidation proceedings under the SIPA is the filing date, and that under § 8–301(1) of the Uniform Commercial Code, title and rights to securities vest in a purchaser at the time of physical delivery, the court held that the broker had never obtained title to the securities, that the title did not vest in the trustee upon delivery of the securities to him, and that the securities never became part of the estate. The court commented that under § 8–309 of the Uniform Commercial Code, the presence of indorsement without delivery of the certificates had no effect upon title. As to certificates which had been delivered prior to the filing date, the court held that title had passed to the broker, and that the shares were a part of the estate in liquidation, the sellers having claims only as general creditors.

[*14] Extension of time for filing claims

In the following case involving liquidation under the SIPA, the court refused to approve a blanket extension of time for filing claims, requested by the trustee, in the absence of a showing that each late claim was meritorious and the delay in filing excusable.

Where the court had initially set a final date for filing proofs of claims in a liquidation proceeding under the SIPA, which date was 59 days after the initial publication of notice of the proceeding in a major newspaper, and where the court thereafter extended the date 33 days at the request of the trustee, the court, in *Securities & Exchange Com. v Kenneth Bove & Co. (1973, DC NY) 353 F Supp 496*, refused to further extend the date an additional 5 1/2 months for all claims filed

between the extended date and the requested final date, notwithstanding the trustee's assertion that the further extension would be in keeping with the policy objectives of the SIPA. The court stated that the application would, in effect, allow payment of claims filed between the extended cutoff date and the absolute limit set by the statute, through incorporation of the applicable provisions of the Bankruptcy Act *(11 U.S.C.A. § 93)*. The court stated that such an absolute outer limit should not be viewed as a normal filing period in SIPA liquidations; that the trustee had presented no special circumstances which might justify the immediate need for a further extension; and that the mere fact that the SIPC may have consented was not dispositive, since the administration of SIPC funds, and payments made therefrom, remained partially under the review and supervision of the District Court. The court stated that should a particular instance arise where a late claim was shown to be meritorious and the delay in filing to be excusable, an application to authorize payment of such claim might be made to the court, but that blanket authority to honor all claims that drift in after an already extended deadline should not be quickly afforded.

Where trustee, in liquidation of broker–dealer under Securities Investor Protection Act, published notice in newspaper, customer of broker–dealer had constructive notice of liquidation proceedings even though he received no notice by mail. Bankruptcy Court did not have discretion to permit filing of late claim in liquidation proceeding under Securities Investor Protection Act where claimant, customer of broker–dealer in liquidation, had received constructive notice of liquidation proceedings through publication of proper notice by trustee. *Re Weis Secur., Inc. (DC NY) 411 F Supp 194*, affd without op (CA2 NY) *538 F2d 313* and affd without op (CA2 NY) *538 F2d 317*.

Notice of proceedings under Securities Investor Protection Act by first class mail is acceptable procedure when balanced with additional costs of other methods of notice. *Re Securities Investor Protection Corp. (DC Minn) 414 F Supp 679*.

[*15] Property rental

In the following case, the court held that the lessor of property leased to a broker–dealer who was placed in liquidation under the SIPA had a valid priority claim against the estate for the period during which the property was utilized by the receiver and trustee.

It was held that a lessor, from whom a broker had leased office space prior to the broker's entering into liquidation proceedings, first under the Bankruptcy Act and then under the SIPA, was entitled to priority rent payment for the period the premises were occupied by the SIPA trustee, and for the prior period during which they were occupied by the bankruptcy receiver, in *Re Buttonwood Secur., Inc. (1972, DC Cal) 349 F Supp 273*, the court pointing out that § 6(c)(2)(B)(ii) of the SIPA *(15 U.S.C.A. § 78fff*(c)(2)(B)(ii)), provides that where necessary the SIPC would advance funds for the payment of certain costs and expenses specified for priority in clauses (1) and (2) of § 64a of the Bankruptcy Act *(11 U.S.C.A. § 104*(a)(1) and (2). The occupancy by the receiver began on the eighth day of the month, and the trustee conceded that the lessor was entitled to administrative rent priority from the period beginning the first day of the following month through the end of the occupancy, but asserted that the applicable rule called for such administrative rent priority not to arise prior to the first date that rent is payable following the filing of a bankruptcy petition on the basis that, as of the rental due date prior to the bankruptcy proceedings, the bankrupt's right to possession of the premises arises for the entire month, as does the landlord's claim for rent, provable in the bankruptcy proceedings. The court stated that it did not fit its concept of justice, nor the intent of the Bankruptcy Act as incorporated in the SIPA, to allow priority payment to other creditors who service the needs of bankruptcy administration while denying it to a lessor who supplies the premises indispensable to the proceedings.

[*16] Unlawful conduct as defeating protection afforded by Act; "clean hands" doctrine

In the following cases, claimants under the SIPA were found to have engaged in unlawful conduct with respect to the transactions leading to their claims, and were held, therefore, not to be eligible for the protection afforded by the Act.

In *Securities & Exchange Com. v Packer, Wilbur & Co. (1973, DC NY) 362 F Supp 510*, affd (CA2) *498 F2d 978*, the court held that a claimant was not entitled to reimbursement out of SIPC funds for losses sustained in a transaction found to have involved an intentional violation of the margin regulations, the court stating that the overriding purpose of the SIPA was best served by prohibiting recovery out of SIPC funds by a customer who wilfully violated the law. The claimant, a customer of both the debtor and a second brokerage, had directed the second brokerage to purchase for him a substantial number of shares of a specified security. The claimant, at about the same time, directed the debtor to sell, on his behalf, an equal number of shares of the same security at a higher price. Both brokerages effected the transactions directed, and the claimant then, without having paid the second brokerage for the shares purchased on his behalf, directed

the second brokerage to deliver the shares to the debtor against the amount due the second brokerage for the shares. The claimant thus attempted to obtain a "free ride" by capitalizing upon the spread in prices while investing no money, a procedure prohibited by margin regulations of the Federal Reserve Board. However, before the claimant could collect from the debtor, the debtor was placed in liquidation, and the claimant contended that his claim should be recognized as a valid one upon the single and separate fund established pursuant to the SIPA. The court rejected the claimant's contention that the violation was inadvertent, pointing out that the claimant had been an active securities trader for many years and should have been familiar with the margin rules, the court adding that it was not a situation wherein the customer inadvertently failed to tender payment for a stock purchase, but rather a situation wherein the claimant had consciously sought to avoid his obligation by effecting the purchase and sale through separate brokers.

In SIPA proceedings involving the liquidation of a broker, the court affirmed the disallowance of a claim based upon the claimant's delivery to the broker of certain securities for which payment had been made with faulty checks where it was found that the claimant had participated with the broker in conspiring to manipulate the price of the securities, in Securities & Exchange Com. v Kelly, Andrews & Bradley, Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94881*, the court stating that upon its face, the "clean hands" doctrine and the claimant's criminal conduct with respect to the stock barred recovery. The court stated that to allow the claimant to obtain reimbursement from public funds for a transaction which was part of his manipulative and fraudulent activities to inflate the price of the stock would be a gross pervasion of a statute intended to protect the victims, not benefit the perpetrators, of such frauds.

Persons who find themselves in position of claimants on special fund established pursuant to Securities Investor Protection Act of 1970 *(15 U.S.C.A. §§ 78aaa* et seq) as result of having violated regulations promulgated pursuant to Securities Exchange Act *(15 U.S.C.A. §§ 78a* et seq) are not intended to be beneficiaries of public funds established pursuant to *SIPA. Securities & Exchange Com. v Provident Secur., Inc. (SD NY) 452 F Supp 477.*

Broker was not entitled to protection of *15 U.S.C.A. § 78fff* based on debtor's repudiation and cancellation of contracts, where debtor repudiated contracts for good and sufficient legal cause, in that debtor honestly and reasonably believed that to perform contract would perpetuate fraudulent scheme, and that contract was void due to securities law violations; further, broker failed to prove qualified customer interest, as required by *15 U.S.C.A. § 78fff*, where broker's ultimate customers in connection with transaction were two dealers, rather than bank, which was in fact acting as agent for dealers, and where dealers' criminal activities disqualified them as "customers." *Re Securities & Exchange Com. (1980, BC SD NY) 2 BR 284.*

[*17] Personal assets of sole proprietor broker–dealer as includible in SIPA liquidation estate

In the following case, the court held that the personal assets of a sole proprietor of a securities brokerage firm were includible in the estate when the firm was placed in liquidation under the SIPA.

In *Securities & Exchange Com. v Wick (1973, DC Ill) 360 F Supp 312*, the court rejected the contention of a trustee, in a liquidation proceeding under the SIPA, that the SIPA had changed the basic concept controlling the liquidation of broker–dealers, and that such a liquidation should be limited to the business assets of a broker–dealer who was a sole proprietor. The court held that the SIPA had superseded the provisions of the Bankruptcy Act only to the extent that the provisions of the Bankruptcy Act would frustrate the ability of the SIPC to protect the funds of customers of broker–dealers, as contemplated by the SIPA. Noting that under the Bankruptcy Act, whether a bankrupt's estate was comprised solely of the available business assets or whether it also encompassed his personal estate depended upon the nature and legal form of the business, the court held that that principle of bankruptcy law was not altered by the SIPA. Pointing out that the broker–dealer's choice of business form was that of a sole proprietorship, the court stated that the broker–dealer was required to accept the liability concomitant with that business form, as recognized under the bankruptcy laws, and that the SIPA trustee was required to deal with both the business and personal assets available to him in the liquidation proceedings. The court commented that such a conclusion was reinforced by the fact that under SEC regulations, the determination of a broker insolvency is predicated, in the case of a sole proprietorship, on the individual's total estate. (For a discussion of the includibility of the personal assets of a sole proprietor broker–dealer in net capital, for purposes of determining whether the broker–dealer is in compliance with the SEC's net capital rule, see the annotation at *19 ALR Fed 9*, § 16[b] .)

[*B] Customers' claims

[*17.] 5 Subordinated creditors

Agreement of subordinated creditor of broker–dealer, in liquidation proceedings under Securities Investor Protection Act, is binding as against creditor with respect to claims of broker–dealer's customers and general creditors; however, if subordinated creditor can show fraud on part of broker–dealer with respect to consummation of subordination agreement, subordinated creditor would take prior to distribution to stockholders of broker–dealer. *Re Weis Secur., Inc. (DC NY) 425 F Supp 212,* (CA2 NY) *605 F2d 590, 24 UCCRS 402.*

See *Securities & Exchange Com. v White & Co. (CA8) 546 F2d 789,* § 18 .

[*18] Who are "customers"

In the following cases, the courts construed the term "customers", as defined in § 6(c)(2)(A)(ii) of the SIPA *(15 U.S.C.A. § 78fff*(c)(2)(A)(ii)).

Customer of broker–dealer in liquidation under Securities Investor Protection Act is only person who has entrusted property to brokerage firm as of filing date. *Securities & Exchange Com. v Security Planners, Ltd. (DC Mass) 416 F Supp 762.*

In *Securities & Exchange Com. v F. O. Baroff Co. (1974, CA2) 497 F2d 280,* the court held that where a voluntary lender of securities to a failing brokerage house had made his loan to help out the company and not for a purpose related to securities trading or investments, he was not a "customer" within the meaning of the SIPA and was therefore not entitled to recover under the Act. The court rejected the lender's claim that he fell within the literal definition of "customer" as set forth in the statute, the lender having pointed out that the statutory definition includes persons who have claims on account of securities received, acquired, or held by the debtor by way of loans of securities by such persons to the debtor. The court stated that the legislative history made it clear that the Act was to protect only investors, and that lenders would therefore be included within the term "customers" only where the loans of securities were made with the intent to use the securities in some type of securities trading or investment activity. The court pointed to the last portion of the definition which excludes a person whose claimed property "by contract, agreement, or understanding, or by operation of law" is part of the capital of the debtor, the court stating that while it was not necessary for it to decide whether such exception applied to the case before it, there was no reason to think that non–investing, non–trading creditors, or gratuitous lenders acting through pure benevolence, family relationship, or friendship, were to be better off under the Act than capital contributors.

It was held that an individual who violated the margin regulations in entering into a transaction with a broker–dealer was not a "customer" of the broker–dealer, for purposes of application of the SIPA, in *Securities & Exchange Com. v Packer, Wilbur & Co. (1974, CA2 NY) 498 F2d 978,* where the court affirmed denial of the broker–dealer's claim that a transaction entered into by the broker–dealer, on behalf of the individual, with the debtor, should be completed as an open contractual commitment. The individual had directed the broker–dealer to purchase a number of shares of a certain security, had simultaneously directed the debtor to sell an equal number of the same securities at a higher price, and then had directed the broker–dealer to deliver the securities purchased on his behalf to the debtor, against payment of the amount owed the broker–dealer on such securities. The debtor had paid for the securities, upon delivery, with faulty checks, and the broker–dealer sought to obtain payment through the requirement, under the SIPA, that the trustee complete open contractual commitments. Observing that open contractual commitments between broker–dealers were required to be completed only where undertaken on behalf of a "customer", and pointing out that the individual had been denied recovery on his own behalf in a previous proceeding, the court stated that the individual was denied the status of a "customer" because upon purchasing the shares through the broker–dealer, he falsely represented, in violation of margin regulations, that he would promptly make full cash payment for the securities, and that he did not contemplate selling the securities prior to making such payment.

Where trust for employees' profit–sharing fund held assets for over 100 employees, and was controlled by three trustees, and where trust maintained account with broker–dealer which was placed in insolvency proceedings under Securities Investor Protection Act, trustees collectively comprised one customer within meaning of Act; individual beneficiaries were not customers. *Securities Investor Protection Corp. v Morgan, Kennedy & Co. (CA2 NY) 533 F2d 1314,* cert den *426 US 936, 49 L ED 2d 387, 96 S Ct 2650.*

Persons who lent securities to securities broker in return for cash collateral equal to market value of shares, those persons retaining right, upon 1 day notice, to demand additional cash if market value of shares should increase and with broker similarly having right to demand return of cash collateral if value of securities declined, were not customers of broker within meaning of § 6(c)(2)(A)(ii) of Securities Investor Protection Act *(15 U.S.C.A. § 78fff*(c)(2)(A)(ii)). *Securities Investor Protection Corp. v Executive Secur. Corp. (CA2 NY) 556 F2d 98.*

Purchaser of subordinated securities is not "customer" of broker–dealer, as defined by predecessor to *15 U.S.C.A. § 78fff*, by virtue of her lack of sophistication in financial dealings, where purchaser conceded that she was aware of high rate of interest on such securities and had received several thousand dollars in interest prior to liquidation of broker–dealer; lender is estopped from rescinding subordination agreement, which was entered into so that broker could comply with regulatory capital requirements, regardless of whether broker's customers relied on such agreement in their dealings with broker. *Re Weis Secur., Inc. (CA2 NY) 605 F2d 590, 4 BCD 532, 17 CBC 529, CCH Bankr L Rptr P 66884, 24 UCCRS 402,* cert den *439 US 1128, 59 L ED 2d 89, 99 S Ct 1045.*

An individual who agreed to sell securities to a brokerage firm, which subsequently was the subject of liquidation proceedings pursuant to the provisions of the SIPA, and who allegedly delivered the securities to a second brokerage firm at the direction of the first firm, was held not to be a customer within the meaning of the Act in *Securities & Exchange Com. v Kenneth Bove & Co. (1974, DC NY) 378 F Supp 697.* The court stated that to have a protected "net equity" claim under the Act as a "customer, " a claimant must have entrusted his securities to the debtor in liquidation, since the Act requires that a claim be on account of securities received, acquired, or held by the debtor, the court concluding that since the debtor never came into possession of the securities or their control, so as to be accountable under the Act to the claimants therefor, the claimant was not a customer under the Act.

Where a claimant had sold shares of a security to the broker in liquidation, and prior to liquidation proceedings had attempted to deliver the securities, but the broker had refused to accept delivery, it was held in Securities & Exchange Com. v Kelly, Andrews & Bradley, Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94881,* that the claim properly had been disallowed by the trustee, since the claimant was not a "customer" within the meaning of the SIPA and, consequently, was not entitled to payment under the Act. The court pointed out that the claimant had never delivered the securities, but had retained them until their sale some time later. The court stated that the loss sustained on that subsequent sale did not constitute a claim on account of securities received, acquired, or held by the debtor, as required in order to be a valid "customer's" claim, the court concluding that the claimant's claim was against the debtor's estate as a general unsecured creditor.

For claimant to be considered customer, under Securities Investor Protection Act, he must have entrusted his securities to debtor in liquidation and, in absence of actual receipt, acquisition or possession of property of claimant by brokerage firm, claimant is not entitled to participation in coverage under Act; where claimant never entrusted securities to firm, but specifically declined to do so and conditioned delivery of stock upon presentation by firm of certified check, and where firm never tendered check and thus never acquired possession of stock, claimant was not customer and claim was required to be disallowed. *Securities & Exchange Com. v E.P. Seggos & Co. (DC NY) 416 F Supp 280.*

Claimants who did not maintain account with brokerage firm which was in liquidation under Securities Investor Protection Act, but lent securities to firm and received cash collateral equal to 100 percent of market value of securities lent, were not customers of firm within meaning of § 6 of Act *(15 U.S.C.A. § 78fff). Securities Investor Protection Corp. v Executive Secur. Corp. (DC NY) 423 F Supp 94,* affd (CA2 NY) *556 F2d 98.*

See *Re Securities & Exchange Com. (1980, BC SD NY) 2 BR 284,* § 16 .

Investor was not entitled to customer status benefits of Securities Investor Protection Act (SIPA) with respect to his claim against bankrupt brokerage, since investor at least knew generally that he was beneficiary of wrongful conduct and, to extent he did not know more details, it was because he closed his eyes to them, and as such, he had level of scienter described in the law as "recklessness." Securities Investor Protection Act of 1970, §§ 1(a) et seq., as amended, *15 U.S.C.A. §§ 78aaa* et seq. *In re Adler, Coleman Clearing Corp., 277 B.R. 520 (Bankr. S.D. N.Y. 2002).*

Investor has "customer" claim, and is entitled to customer protection under the Securities Investor Protection Act (SIPA), as long as he was owed property by broker on the SIPA filing date; mere fact that this property is missing, perhaps due to unauthorized trading, does not affect his "customer" status. Securities Investor Protection Act of 1970, § 16(2, 4), as amended, *15 U.S.C.A. § 78lll*(2, 4). *In re Klein, Maus & Shire, Inc., 301 B.R. 408 (Bankr. S.D. N.Y. 2003).*

Bank, which had guaranteed forged signatures on securities without notice of broker's fraudulent conversion of those securities, and which took assignment of defrauded customers' claims in return for delivering new certificates to customers, was not entitled to preferred status of customer under Securities Investor Protection Act, but merely had status of general creditor since bank's claim's merits were quite different than if bank had purchased customers' interest with funds that it was not otherwise required to expend. *Securities & Exchange Com. v Albert & Maguire Secur. Co. (CA3) 560 F2d 569.*

As result of conversion by bankrupt broker of stock it was contractually required to deliver to purchaser, purchaser was "customer" within meaning of § 6(c)(2)(A)(ii)of Securities Investor Protection Act *(15 U.S.C.A. § 78ff*(c)(2)(A)(II)), but that mere fact did not mean that customer had enforceable preferred claim; bank which had guaranteed signatures on certificates, and which purchased and delivered to purchaser replacement certificates and thereupon received assignment of purchaser's claim as customer against bankrupt's estate, could not assert claim under Act since customer could have enforced rights against issuing corporation requiring corporation to issue replacement certificates. *Re Albert & Maguire Secur. Co. (DC Pa) 419 F Supp 1171.*

In order for claimant to qualify for protection under the Securities Investor Protection Act (SIPA) as "customer" of bankrupt broker/dealer, (1) the transactions in which claimant engaged, and which form basis of his/her claimed customer status, must relate to investment, trading or participation in securities market, and (2) transactions must have arisen out of type of fiduciary relationship which generally characterizes relationship between a broker–dealer and its customers. Securities Investor Protection Act of 1970, § 16(2), as amended, *15 U.S.C.A. § 78*<emph type="if">lll<endemph type="if">(2). *In re First Interregional Equity Corp., 290 B.R. 265, Fed. Sec. L. Rep. (CCH) P 92297 (Bankr. D. N.J. 2003).*

In determining nature of claimant's status in relationship to debtor broker–dealer, court must look to matters as they existed on filing date of liquidation proceeding; claimant who purchased two investment certificates from corporation formed for purpose of making loans to bond purchasers, which corporation was alter ego of debtor, and whose investment was to have been used by corporation to defray cost of organizing company and to make installment loans to individuals desiring to purchase religious institutional bonds was not customer of debtor within meaning of *15 U.S.C.A. § 78fff*(c)(2)(A)(ii), since she had not entrusted securities to debtor, and had not left cash with debtor for purpose of purchasing securities. *Re Atkeison (MD Tenn) 446 F Supp 844.*

Term "customer," as used within the Securities Investor Protection Act (SIPA), is not meant to simply refer to one who buys, sells, or trades securities but, rather, is a term of art meant to be a shorthand designation for those eligible to receive special protection for their investments. Securities Investor Protection Act of 1970, §§ 1(a) et seq., *15 U.S.C.A. §§ 78aaa* et seq. *In re John Dawson & Associates, Inc., 271 B.R. 561 (Bankr. N.D. Ill. 2001).*

Since term "customer," within meaning of § 6 of Securities Investor Protection Act *(15 U.S.C.A. § 78fff),* does not include any person to extent that such person has claim for property which by contract, agreement, or understanding, or by operation of law, is part of capital of debtor or is subordinated to claims of creditors of debtor, shareholder of brokerage in liquidation which shareholder had by series of subordination agreements lent securities to firm for number of years, which were in effect at time of liquidation, was not customer of firm within meaning of Act. *Securities & Exchange Com. v White & Co. (CA8) 546 F2d 789.*

Bank, which inadvertently overpaid broker–dealer, which subsequently was placed in liquidation under Securities Investor Protection Act, did not deposit cash with broker–dealer for purpose of purchasing securities, within meaning of Act, and therefore was not "customer" under *15 U.S.C.A. § 78fff*(c)(2)(A)(ii). *Securities & Exchange Com. v White & Co. (DC Mo) 406 F Supp 806.*

Investor is "customer," entitled to protection under the Securities Investor Protection Act (SIPA) and to compensation from the Securities Investor Protection Corporation (SIPC), only if he/she entrusted cash or securities with the now insolvent broker–dealer, and only if such cash was deposited for the purpose of purchasing securities. Securities Investor Protection Act of 1970, § 16(2), as amended, *15 U.S.C.A. § 78lll*(2). *In re Primeline Securities Corp., 295 F.3d 1100, 39 Bankr. Ct. Dec. (CRR) 211 (10th Cir. 2002).*

Claimant can recover under Securities Investor Protection Act if he fits customer definition in *15 U.S.C.A. § 78fff*(c)(2)(A)(ii); customers are persons who have claims on account of securities received, acquired, or held by stockbroker; preferential protection of Act is accorded to persons who can trace and identify property or funds in hands of broker, but otherwise claimant must look to general assets of stockbroker for satisfaction. *Securities Investor Protection Corp. v Associated Underwriters, Inc. (DC Utah) 423 F Supp 168.*

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The court held that a claim based upon alleged fraud on the part of an insolvent broker was not a "customer claim" within the meaning of the SIPA, in *Securities & Exchange Com. v S. J. Salmon & Co. (1974, DC NY) 375 F Supp 867,* the court upholding the bankruptcy court's sustaining of the trustee's objections to the claim filed. The customer originally

alleged that the broker, at his direction, had sold securities owned by the customer and had used the proceeds to make an unauthorized purchase of a different stock. In the alternative, the customer asserted that the authorization to purchase the different stock had been obtained through the broker's fraud. The court stated that had the purchase of the different stock been unauthorized, the customer would have had a valid claim in the amount of the sale price of the original stock, since, under the Act, customers are to be reimbursed if their property has been lost or misappropriated by a broker. However, the court stated that since the bankruptcy court had found that the subsequent purchase had been authorized, the customer was required to pursue his fraud claim as a general creditor and look for satisfaction to the broker's general estate, not to the single and separate fund.

[*19] Net equity claims

In the following cases the courts, in ruling upon the validity of claims for net equity payments under *15 U.S.C.A. § 78fff*(g), have discussed what comprises "net equity" within the meaning of *15 U.S.C.A. § 78fff*(c)(2)(A)(iv).

Money paid for certificates of deposit and for letters of credit of banks which subsequently were placed in receivership was held not to be includible in the net equity of the purchaser's account with the broker through whom the transaction was consummated, in *Securities & Exchange Com. v C. H. Wagner & Co. (1974, DC Mass) 373 F Supp 1214,* where the court overruled customers' objections to the trustee's disallowance of claims under the SIPA based upon such investments. The customers had paid for the certificates of deposit and letters of credit pursuant to a scheme, devised by the broker, whereunder the customers were to receive "bonus interest" for their investments. The broker arranged for banks, upon receipt of payment for the certificates of deposit and letters of credit, to lend the proceeds to substandard borrowers, who would then pay the broker a commission or finder's fee, part of which was paid by the broker to the customers as their "bonus interest." The broker transmitted the customers' funds to the banks and paid the "bonus interest" to the customers, but the banks were placed in receivership prior to their issuance of the certificates of deposit, although the letters of credit had been issued. Since the banks were to have sent the securities directly to the customers, there was no further action to be taken by the broker, and the court held that the funds which had been transmitted to the banks were not funds to be included in the customer's net equity under the Act.

Under Securities Investor Protection Act (SIPA), customers' net equity claims for securities are satisfied with securities, whereas cash net equity claims are satisfied with cash. Securities Investor Protection Act of 1970, § 1(a), as amended, *15 U.S.C.A. §§ 78aaa* et seq. *In re Stratton Oakmont, Inc., 257 B.R. 644 (S.D.N.Y. 2001).*

In *Securities & Exchange Com. v Aberdeen Secur. Co. (1973, CA3 Del) 480 F2d 1121,* cert den *414 US 1111, 38 L Ed 2d 738, 94 S Ct 841,* the court stated that a customer's net equity, under the SIPA, consisted of both his cash balance and his securities account valued as of the filing date, the court remanding for reconsideration of whether there had been a claim for cash properly falling within the customer's net equity. The customer had subscribed, through the broker in liquidation, for shares of a prospective new issue. The purchase was confirmed by the broker and paid for by the customer in the form of a credit from his account. The prospective issuer went into bankruptcy without issuing the shares, and the broker was placed in liquidation under the SIPA without having reimbursed the customer. Stating that the District Court, in its determination that the customer had no net equity, had not correctly considered the definition of that term, the Court of Appeals stated that if, under local law or by virtue of regulations under which it operated, the broker was obligated to refund to the customer the amount paid for the unissued stock, that amount would be included in the customer's net equity. The court therefore directed the District Court to resolve that factual question.

And see *Securities & Exchange Com. v Aberdeen Secur. Co. (1974, DC Del) 371 F Supp 1343,* where a brokerage firm, prior to being placed in liquidation under the SIPA, had sent a check to a customer to cover the customer's credit balance, but the customer had never cashed that check, and where the court held that the amount owing to the customer, as represented by the check, was specifically identifiable property (see § 22 , infra), but that if it should not be considered to be that, it constituted "net equity" in the customer's account.

[*20] —Cash claims subject to limitation of payment from SIPC fund

In the following case, the court found that a claimant's claim was one for cash and that the limitation for payments made out of the SIPA funds, as contained in *15 U.S.C.A. § 78fff*(f)(1)(A), was applicable.

Where it was found, contrary to a claimant's assertions, that the claimant had delivered securities to a broker in liquidation for resale by the broker, and that the broker had purchased the securities, the court held that the claimant's claim was for cash, in Re Weis Secur., Inc. (1974, DC NY) *CCH Fed Secur. L Rep P 94780,* the court concluding that since

payment was to be made from the SIPC fund, the claimant was entitled to no more than the statutory limit of $20,000.

[*21] Open contractual commitments
[*21a] Text of SEC Rule

Under § 6(d) of the SIPA *(15 U.S.C.A. § 78fff*(d)), the requirement that a trustee complete certain "open contractual commitments" is dependent partly upon the Securities and Exchange Commission's determining, "by rule or regulation," that the completion of such commitments is or is not "in the public interest." Pursuant to these statutory provisions, the SEC has promulgated the following rule (17 CFR § 240.206d–1):

§ 240.206d–1. Completion of open contractual commitments.

(a) Definitions.For the purpose of this section, adopted pursuant to subsection 6(d) of the Securities Investor Protection Act of 1970 (hereinafter referred to as "the Act"):

(1) The term "failed to receive" shall mean a contractual commitment of the debtor made in the ordinary course of business, to pay to another broker or dealer the contract price in cash upon receipt from such broker or dealer of securities purchased, provided that the respective obligations of the parties remained outstanding until the close of business on the filing date as defined in section 5(b)(4)(B) of the Act (hereinafter referred to as the "filing date").

(2) The term "failed to deliver" shall mean a contractual commitment of the debtor, made in the ordinary course of business, to deliver securities to another broker or dealer against receipt from such broker or dealer of the contract price in cash, provided that the respective obligations of the parties remained outstanding until the close of business on the filing date.

(3) The term "open contractual commitment" shall mean a failed to receive or a failed to deliver which had a settlement date prior to the filing date and the respective obligations of the parties remained outstanding on the filing date or had a settlement date which occurs on or within five business days subsequent to the filing date: Provided, however, That the term open contractual commitment shall not include any contractual commitment for which the security which is the subject of the trade had not been issued by the issuer as of the trade date.

(4) The term "customer" shall mean a person (other than a broker or dealer) in whose behalf a broker or dealer has executed a transaction out of which arose an open contractual commitment with the debtor, but shall not include any person to the extent that such person at the filing date (i) had a claim for property which by contract, agreement or understanding, or by operation of law, was a part of the capital of the broker or dealer who executed such transaction or was subordinated to the claims of creditors of such broker or dealer, or (ii) had a relationship with the debtor which is specified in section 6(f)(1)(C) of the Act, or had a corresponding relationship with such other broker or dealer.

(b) It is hereby determined to be "in the public interest," within the meaning of section 6(d)(2) of the Act, for a trustee to complete such open contractual commitments as are specified in paragraph (c) below in accordance with the procedures prescribed in this section, irrespective of whether a customer did or did not have an interest therein; and, except as otherwise provided in paragraphs (h) and (i), it is also hereby determined to be "not in the public interest," within the meaning of section 6(d)(1) of the Act, for a trustee to complete such open contractual commitments as are described in paragraph (a)(3), other than those specified in paragraph (c).

(c) An open contractual commitment shall be completed if:

(1) The open contractual commitment:

(i) Arises from a transaction in which a customer (as defined in this rule) of the other broker or dealer had an interest. For purposes of this rule a customer is deemed to have an interest in a transaction if (A) the other broker was acting as agent for the customer or (B) the other dealer was not a market maker in the security involved, to the extent such other dealer held a firm order from the customer and in connection therewith: In the case of a buy order, prior to executing such customer's order purchased as principal the same number of shares or purchased shares to accumulate the number of shares necessary to complete the order; or in the case of a sell order, prior to executing such customer's order sold the same number of shares or a portion thereof; and

(ii)

(A) Had a settlement date on or within 30 calendar days prior to the filing date and the respective obligations of the parties remained outstanding on the filing date or had a settlement date which occurs on or within five business days subsequent to the filing date; and

(B) Had a trade date on or within five business days prior to such settlement date; and

(2) the other broker or dealer can establish to the satisfaction of the trustee through appropriate documentation that:

(i) In the case of a broker or dealer who maintains his records on a specific identification basis:

(A) The open contractual commitment arose out of a transaction in which his customer had such an interest, and

(B) In the case of a failed to deliver of the debtor, as of the filing date such broker's or dealer's customer's interest had not been sold to such broker or dealer; or

(ii) In the case of a broker or dealer who maintains his records other than on a specific identification basis, that he has determined that a customer had such an interest in a manner consistent with that used by such broker or dealer prior to the filing date to allocate fails to receive and fails to deliver in computing the special reserve bank account requirement pursuant to the provisions of Rule 15c3–3 under the Securities Exchange Act of 1934; or

(iii) In the case of a broker or dealer not described in paragraph (c)(2)(i) or (ii) of this section that he has made the determination in a manner which the trustee finds to be fair and equitable.

(d)

(1) The completion of an open contractual commitment meeting the requirements of paragraph (c) of this section shall be effected only:

(i) By the buy–in or sell–out of the commitment by the other broker or dealer in accordance with the usual trade practices initiated by the other broker or dealer within or promptly upon the expiration of a period of 30 calendar days after settlement date; or

(ii) At the option of the trustee by the delivery of securities against receipt of the contract price or payment of the contract price against the receipt of securities at any time within thirty calendar days after settlement date unless the commitment previously has been bought–in or sold–out in accordance with paragraph (d)(i)(ii) of this section; or

(iii) In the event of the refusal of the other broker or dealer to accept completion of an open contractual commitment in accordance with paragraph (d)(1)(ii) of this section, or the failure of the other broker or dealer to promptly buy–in or sell–out a commitment in accordance with paragraph (d)(1)(i) of this section, or in the event of the failure of the other broker or dealer to provide the trustee with appropriate documentation as required by this section, by delivery of securities against receipt of the contract price or payment of the contract price against receipt of securities, or the buy–in or sell–out of the commitment or cancellation of the commitment or otherwise, as may be appropriate, as the trustee in his discretion believes will most benefit the estate of the debtor.

(2) In the event of a close–out of an open contractual commitment pursuant to paragraph (d)(1)(i) of this section, the money difference resulting from such close–out shall be payable by the other broker or dealer to the trustee or by the trustee to the other broker or dealer, whichever would be entitled to receive such difference under the usual trade practices: Provided, however,

(i) That prior to the payment of any such money difference by the trustee to such other broker or dealer with respect to transactions executed by such other broker or dealer for any separate customer account, all open contractual commitments with respect to such account which meet the requirements of paragraph (c) of this section must have been completed by the delivery of securities against receipt of the contract price, or by payment of the contract price against receipt of the securities in conformity with paragraph (d)(1)(ii) of this section, or by buy–in or sell–out in conformity with paragraph (d)(1)(i) of this section, and

(ii) that the net amount so payable by the trustee to the other broker or dealer shall not exceed $20,000 with respect to any separate customer account.

(e)

(1) As soon as practicable after publication pursuant to Section 6(e) of the Act of notice of the commencement of proceedings, a broker or dealer who has executed transactions out of which arose open contractual commitments with the debtor shall furnish to the trustee such information with respect to all open contractual commitments meeting the requirements of paragraph (c) of this section (including any of such commitments which have been bought–in or sold–out by the broker or dealer), as called for by Forms S6(d)A–1 and S6(d)A–2 (17 CFR 249a.6d–1, 249a.6d–2 of this chapter) including appropriate supporting documentation.

(2) Promptly upon the expiration of 45 calendar days after the filing date, or if by the expiration of such 45–day period notice pursuant to section 6(e) of the Act of the commencement of proceedings has not been published, then as soon as practicable after publication of such notice, a broker or dealer who had executed transactions in securities out of which arose open contractual commitments with the debtor shall furnish to the trustee such information with respect to the buy–in, sell–out or other status of open contractual commitments meeting the requirements of paragraph (c) of this section as called for by Forms S6(d)B, S6(d)C–1 and S6(d)C–2 (17 CFR 249a.6d–3, 249a.6d–4a1, and 249a.6d–4a2) including appropriate supporting documentation, and schedules.

(f)

(1) Nothing stated in this section shall be construed to prejudice the right of a broker or dealer to any claim against the debtor's estate, or the right of the trustee to make any claim against a broker or dealer, with respect to a commitment of

the debtor which was outstanding on the filing date, but (i) which is not described in paragraph (a)(3) of this section, or (ii) which, although described in paragraph (a)(3) of this section, does not meet the requirements specified in paragraph (c) of this section or was not completed in accordance with paragraph (d) of this section or was not reported to the trustee in conformity with paragraph (e) of this section or was not supported by appropriate documentation.

(2) Nothing stated in this section shall be construed to prejudice the right of a broker or dealer to a claim against the debtor's estate for the amount by which the money difference due the broker or dealer upon a buy–in or sell–out may exceed the amount paid by the trustee to such broker or dealer.

(g) Notwithstanding the fact that an open contractual commitment describe in paragraph (a)(3) of this section meets the requirements of paragraph (c) of this section and the other requirements of this section, a Court shall not be precluded from canceling such commitment, awarding damages, or granting such other remedy as it shall deem fair and equitable if, on application of the trustee or the Securities Investor Protection Corporation ("SIPC"), it determines that such commitment was not entered into in the ordinary course of business or was entered into by the debtor, or the broker or dealer or his customer, for the purposes of creating a commitment in contemplation of a liquidation proceeding under the Act. Such a determination shall be made after notice and opportunity for hearing by the debtor, such broker or dealer, or such customer, and may be made before or after the delivery of securities or payment of the contract price or before or after any buy–in or sell–out of the open contractual commitment, or otherwise.

(h) Upon application to the Commission by SIPC or the trustee or upon its own motion, the Commission may, after notice and opportunity for hearing by interested persons find it to be in the public interest, in order to prevent a substantial detrimental impact upon the financial condition of one or more brokers or dealers, for the trustee to complete an open contractual commitment, irrespective of whether it is described in paragraph (a)(3) of this section or meets the requirements of paragraph (c) of this section or has been reported in conformity with paragraph (e) of this section, or is supported by appropriate documentation.

(i) Nothing contained in this section shall be construed as affecting in any way the power of the trustee (1) to complete, in such manner as may be approved by the Court, an open contractual commitment of the debtor not described in paragraph (a)(3) of this section the completion of which, apart from this section, is authorized or required by section 6(d) of the Act, or (2) to complete an open contractual commitment of the debtor, regardless of whether it is described in paragraph (a)(3) of this section or meets the requirements of paragraph (c) of this section or has been reported to the trustee in conformity with paragraph (e) of this section, to the extent that such commitment is completed with property which constituted specifically identifiable property on the filing date of the customer of the debtor for whose account the commitment was made, or was paid or delivered by or for the account of such customer to the debtor or trustee after the filing date.

[*21b] Judicial construction

In the following cases, the courts have construed the term "open contractual commitments," as used in § 6(d) of the SIPA *(15 U.S.C.A. § 78fff*(d)).

The court pointed out that open contractual commitments, within the meaning of the SIPA, were those of the debtor, the insolvent broker, which were outstanding on the filing date, in *Securities & Exchange Com. v C. H. Wagner & Co. (1974, DC Mass) 373 F Supp 1214*, where the court, in overruling the objections by customers of an insolvent broker to the trustee's disallowance of their claims under the SIPA, pointed out that the contractual obligations owed the customers were primarily those of the issuers of the securities. The broker had set up a system whereunder he would obtain investors to purchase certificates of deposit or letters of credit from banks, and the banks would lend the proceeds to a substandard borrower, who would then pay a substantial commission or finder's fee to the broker. A part of such commission was then paid to the investors, such payment, called the "bonus interest" or "discount," being the investors' inducement to enter into the transaction. Upon the broker's transmittal of payment to the banks, the banks were to send the certificates of deposit or letters of credit directly to the customers, but prior to the receipt by the customers of some of the certificates of deposit due, the banks were placed in receivership. Noting that the open contractual commitment provisions of the Act were designed for the protection of customers trading in readily marketable securities such as stocks and bonds, the court pointed out that in the ordinary course of a broker's business in handling such transactions, the broker often receives payment for securities before the securities are in deliverable form, in which case the broker holds the customers' funds until delivery of the securities. The court stated that it is that type of open contractual commitment which the SIPA trustee is obliged to complete, and that where no further action need be taken by the broker, there is generally no open contractual commitment within the meaning of the Act.

Provisions relating to open contractual commitments, as contained in § 6(d) of Securities Investor Protection Act *(15 U.S.C.A. § 78fff*(d)) were designed to deal not with all orders placed with insolvent broker but rather with those involving

inter–broker orders which were not complete on date of filing; further, all such inter–broker orders do not fall within scope of provisions and trustee properly disallowed claim which involved failure to receive in excess of 30 days prior to filing date; § 6(d) does not allow brokers to sit back in event of failure to receive and come to SIPC for payment out of funds supplied by industry. *Securities & Exchange Com. v Security Planners, Ltd. (DC Mass) 416 F Supp 762.*

The court stated that a broker–dealer can claim the protection of the SIPA only to the extent that it was acting on behalf of its own customers in dealing with a defunct firm, in *Securities & Exchange Com. v Packer, Wilbur & Co. (1974, CA2 NY) 498 F2d 978,* where the court affirmed denial of a broker's claim, in a liquidation under the SIPA, based upon an alleged open contractual commitment. A customer of both the claimant and the debtor (the brokerage in liquidation) had directed the claimant to purchase for him a substantial number of shares of a specified security. The customer also directed the debtor to sell, on his behalf, an equal number of shares of the security at a higher price, and then, without having paid the claimant for the shares purchased, directed the claimant to deliver those shares to the debtor, against payment of the amount due the claimant for the shares. The debtor paid for the securities with faulty checks, and the claimant sought to be paid on the basis of the trustee's duty to complete contractual commitments under the Act. The court pointed out that the customer, in an earlier action, had been denied the status of a "customer" under the Act because, upon purchasing the shares through the claimant, he falsely represented, in violation of margin requirements, that he would promptly make full cash payment for the security and that he did not contemplate selling the security prior to making such payment. The court concluded that, since § 6(d)(1) of the Act *(15 U.S.C.A. § 78fff*(d)(1)) provides that only those open contractual commitments shall be completed in which a "customer" has an interest, the transaction which the claimant sought to have completed did not qualify, since the customer did not qualify as such within the meaning of the Act. The court further stated that the dishonored checks did not represent an open contractual commitment under § 6(d) of the Act, because the framers of the SIPA understood the term "open contractual commitment" to mean a wholly executory contract.

**** Caution:

Although the court in Securities & Exchange Com. v Packer, Wilbur & Co., supra, affirmed the District Court's decision *(362 F Supp 510),* it did not concur with the District Court's reasoning as to why the claimant's claim should be denied. The District Court had based its decision upon the conclusion that the claimant had violated the margin regulations, or had breached some duty of care imposed by such regulations, when it delivered the securities to the debtor without first receiving payment, thereby allowing the customer to obtain a free ride. The Court of Appeals stated that such regulations did not prohibit free riding, but simply imposed a foreclosure on other credit or delayed–payment transactions if a free ride or other premature sale had occurred within the preceding 90 days, the court concluding that the claimant's delivery of the unpaid–for stock, at the customer's request, did not appear to violate the regulations.

In *Securities & Exchange Com. v Kenneth Bove & Co. (1974, DC NY) 378 F Supp 697,* where an individual agreed to sell securities to a brokerage firm and allegedly delivered the securities to a second brokerage firm at the direction of the first firm, the court held that the individual could not, in liquidation proceedings of the first firm under the SIPA, require payment for the securities as completion of an open contractual commitment. The court stated that the term "open contract," as used in the Act, is a term of art in the brokerage business, and that it is understood in the brokerage community to refer to "street" obligations. Stating that the terms in the statute must be read with an understanding and awareness of the language and context of the brokerage business, since the Act was a statute relating only to that particular industry, the court held that the open contractual commitment provisions of the Act were clearly intended to apply only to open contractual commitments that exist between a broker or dealer–debtor and another broker or dealer, the purpose of the "open contract" provisions of the Act being said to secure the completion of street obligations and not open transactions of a broker with members of the public.

Where a broker had transferred a customer's account to a second broker in consideration of payment of the debit balance of the account, the transfer occurring after the announcement of a stock split applicable to the stock held in the account, but prior to the distribution of the additional shares, and where the transferor broker was placed in liquidation proceedings under the SIPA without having received the additional shares, the court in Seidman v Weis Secur., Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94757,* refused to direct the trustee to pay the value of the additional shares to the customer's account with the second broker under the "open contractual commitment" provisions of the Act. The debtor broker never received the additional shares, allegedly because of the second broker's failure to present a due bill for the shares as required in the distribution procedure, and the customer had been paid $50,000 by the SIPC for his loss of the stock. The court stated that it was not the purpose of § 6(d) of the SIPA *(15 U.S.C.A. § 78fff*(d)) to benefit creditors such as the customer, the court adding that Congress intended the Act to protect all creditors of financially disabled investment

houses equally.

Where a claimant, in a liquidation proceeding under the SIPA, had delivered securities to the broker in liquidation, and the broker had subsequently purchased those securities prior to the initiation of the liquidation proceedings, but the claimant alleged that there was no legal transfer of the securities because the real purchaser was not the broker but an investment company on whose behalf the broker had acted, the court in Re Weis Secur., Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94780,* declined to require the completion of the asserted "open contractual commitment" with the investment company pursuant to the requirements of *15 U.S.C.A. § 78fff*(d). The court stated that the Act required completion of only those contracts in which the customer had an interest, or, where customers had no interest, where the Securities and Exchange Commission determined that the completion of the contract was in the public interest, neither of which conditions was said to be met in the instant case.

Where a broker in liquidation under the SIPA had refused to accept delivery of securities pursuant to a contract with the claimant, and the claimant had subsequently sold the securities elsewhere at a loss, the contract between the claimant and the broker was held not an open contractual commitment within the meaning of § 6(d) of the SIPA *(15 U.S.C.A. § 78fff*(d)), and the trustee was held properly to have refused to complete the alleged contract, in Securities & Exchange Com. v Kelly, Andrews & Bradley, Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94881.* The court stated that the section contemplated completion by the trustee of outstanding executory contracts between brokers, but that there had been no executory contract outstanding as of the filing date, since the debtor had previously breached the contract by refusing to accept the securities, and the claimant had sold to another broker, the debtor–broker therefore no longer being under a commitment to accept the securities, and the claimant being under no obligation to deliver them. The court stated that the claimant's claim was merely one for damages for breach of contract. The court further stated that the trustee had also properly refused to complete an alleged open contractual commitment where the debtor–broker had refused to accept securities from a second claimant, even though the second claimant had not subsequently sold the securities. Although the second claimant contended that the transaction remained open because it could not sell the securities, since the debtor–broker was the primary market maker in the stock and there was no other way to sell the shares, the court pointed out that the quotation sheets of the National Association of Securities Dealers indicated to the contrary, and that the second broker could have sold the shares after the debtor–broker had breached its agreement of purchase, and, further, that the second broker was required to do so to mitigate its losses. The court stated that SEC policy and general industry practice were that in the instance of a breach of contract by a purchasing broker, the selling broker should sell the securities and close out the transaction. The court added that even if there were no market after the date of the breach, the debtor–broker's refusal to accept delivery gave rise to a claim for breach of contract for the resulting damages, and that even then, the transaction would not come within the definition of an open contractual commitment under § 6(d) of the Act. Moreover, the court stated that the purpose of § 6(d) of the Act, calling for the trustee's completion of open contractual commitments, was to avoid the so–called "domino effect" whereby the insolvency of one broker could cause the collapse of another because of the former's inability to complete open transactions, by the payment of cash or the delivery of securities.

Clearing agreement between introducing broker and bankruptcy clearing firm, which did not purport to define terms of any particular customer's trade or the conditions relating to establishment and servicing of any individual customer's account, was not "contract for sale or purchase" of securities from account, such as might support claim for securities under the Securities Investor Protection Act (SIPA) by customers that broker had introduced to firm, as alleged third–party beneficiaries of this clearing agreement. Securities Investor Protection Act of 1970, § 1(a) et seq., *15 U.S.C.A. § 78aaa* et seq.; 17 C.F.R. § 300.502(a)(2). *In re Adler, Coleman Clearing Corp., 263 B.R. 406 (S.D.N.Y. 2001).*

Even if option contracts, whereunder broker–dealer, acting as dealer, sold options through separate contracts with sellers and buyers, were open contractual commitments within meaning of § 6 of Securities Investor Protection Act *(15 U.S.C.A. § 78fff),* trustee "completed" contracts when he recognized them as valid, noted their exercise, and acknowledged money claims resulting therefrom; however, even if they were not "completed", option customers could not assert claim under Act because they were not in class protected by statutory provision, which applies only to contracts between debtor and another broker–dealer and not to contracts between debtor and customer, since there was no agreement between broker–dealer and option customers (customers who sold options through broker–dealer, acting as dealer) whereunder broker–dealer was obligated to provide notice to customers of exercise of options, trustee of broker–dealer in liquidation proceedings under Securities Investor Protection Act was not obligated to give such notice. *Re Weis Secur., Inc. (DC NY) 411 F Supp 195.*

In *Securities & Exchange Com. v Aberdeen Secur. Co. (1973, CA3 Del) 480 F2d 1121,* cert den *414 US 1111, 38 L Ed*

2d 738, 94 S Ct 841, it was found that an "open contractual commitment," as contemplated by the SIPA, did not exist and that the trustee should not, therefore, be compelled to make a purchase of securities necessary to complete a contract with the debtor's customer, the court stating that open contractual commitments do not encompass undertakings involving only the broker–dealer and his customer, but that open contractual commitments covered by the Act are only those between a broker–dealer and another broker–dealer. The customer had placed an order with the debtor for a number of shares of a specified stock and had remitted the full purchase price. Upon the debtor's being placed in liquidation proceedings under the SIPA, it was found that the broker had an insufficient number of shares of the stock to satisfy its obligations to all the customers to whom it owed such stock. The trustee proposed to pay to the customer his pro rata share of the stock available in the liquidation estate, plus a cash payment for the shares of stock which could not be provided out of the estate. The court, rejecting the customer's contention that the trustee was required to obtain additional stock and deliver the total quantity called for under the contract between the customer and the debtor, noted that, at the time of the enactment of the SIPA, the securities industry was concerned with the "domino effect" of the financial difficulties of one broker extending to others with whom he dealt, and that the industry desired to confine the problems to the one who was insolvent. Noting that there was also sentiment to limit the protection of the SIPA to customers and not to extend it to transactions between brokers, the court stated that the compromise ultimately agreed upon was to provide for the completion of interbroker or interdealer transactions when the interest of a customer on either side is involved.

**** Comment:

The court in *Securities & Exchange Com. v Aberdeen Secur. Co., supra,* noted that discretion was left to the SEC to promulgate rules which would allow completion of transactions in which customers did not have an interest, if this was determined to be in the public interest. (For the text of the SEC rule promulgated with respect to open contractual commitments, see § 21[a] , supra.)

Where a securities broker held securities which customers had purchased on margin, and pledged such securities for a loan, it was held in *Securities & Exchange Com. v Albert & Maguire Secur. Co. (1974, DC Pa) 378 F Supp 906,* that in liquidation of the broker's business under the SIPA, the customers were not entitled, under the open contractual commitment provisions of the SIPA, to pay the amounts owing on the securities and to receive the proceeds of sales of the securities which had been effected by the trustee. The court stated that the term "open contractual commitments of the debtor," within the meaning of the Act, refers not to the relationship of the debtor–broker with a margin customer, but rather to the relationship of the debtor with another broker–dealer.

[*22] Specifically identifiable property

Under § 6(c)(2)(C) of the SIPA *(15 U.S.C.A. § 78fff*(c)(2)(C)), the trustee in a liquidation proceeding is required to return "specifically identifiable property" to the customers of the debtor. In the following cases, the courts have construed the term "specifically identifiable property," within the meaning of that requirement.

Where a broker sold a customer's holdings in a particular stock, and then, allegedly through fraudulently obtained authority, used the proceeds to purchase a different stock, the court in *Securities & Exchange Com. v S. J. Salmon & Co. (1974, DC NY) 375 F Supp 867,* stated that the customer had a valid claim, under the SIPA, for the stock in the second corporation as specifically identifiable property.

It was held that a claim for credit for stock, based upon the stock's being specifically identifiable property, could not be maintained where the debtor never had possession of the stock, in Seidman v Weis Secur., Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94757.* In order to satisfy a debit balance in the claimant's account, the debtor had transferred to a second broker, in consideration for payment of the debit balance, the claimant's account containing a number of shares of a particular stock, the transfer being accomplished after the issuer of the stock had announced a stock split, but prior to the delivery date for the additional shares. The additional shares were to be distributed pursuant to presentation of due bills, through a stock–clearing corporation. The second broker did not present a due bill to the debtor for the additional shares, as the trustee alleged it should have, and before the transfer could be effected, the debtor was placed in liquidation proceedings under the SIPA. The court concluded that the debtor never had anything more than a credit on its books for the stock due the second broker, and that it therefore never had shares particularly identifiable to the claimant. The court noted that the debtor had redeemed due bills for the same class of stock from other brokers, and that the trustee held cash received for those assets, but the court held that no property originally owned by the claimant was commingled with that cash, and that none of the cash was specifically identifiable within the meaning of § 6(c)(2)(C) of the SIPA *(15 U.S.C.A. § 78fff*(c)(2)(C)).

Where it was found, in a liquidation proceeding under the SIPA, that the claimant had delivered securities to the broker for the purpose of having the broker sell such securities, and that the broker had thereupon purchased the securities, the court in Re Weis Secur., Inc. (1974, DC NY) *CCH Fed Secur L Rep P 94780*, held that the claimant did not have the right to have the securities returned as specifically identifiable property. However, the court, denying the trustee's affirmative defense that the claimant had failed to state a cause of action upon which relief could be granted, stated that if the claimant could prove that the securities had merely been deposited with the broker for safekeeping or that the broker had been guilty of fraud in inducing the sale, despite his being on the brink of termination of operations, the claimant would have been able to prevail.

Where there is specifically identifiable property of many customers in estate of broker–dealer in liquidation under Securities Investor Protection Act, but not enough shares to permit delivery of that property, trustee is permitted, under § 6(c) of Act *(15 U.S.C.A. § 78fff*(c)), to make pro rata delivery and make payment in cash for any shortages; where customer receives such cash credit for undelivered shares, he has no entitlement to dividends or "rights" in respect of those shares. *Re Weis Secur., Inc. (DC NY) 411 F Supp 195.*

Where a customer of a brokerage firm, which subsequently was placed in liquidation under the SIPA, was shown in the firm's ledger sheet as having a credit balance of $946, and where the brokerage had sent him a check in that amount intending it to be full payment of the credit balance, but where the customer never presented the check for payment nor provided the brokerage with any explanation as to why he continued to hold it, the court in *Securities & Exchange Com. v Aberdeen Secur. Co. (1974, DC Del) 371 F Supp 1343*, held that the customer was entitled to receive payment of the money as specifically identifiable property within the meaning of the Act. The court stated that "specifically identifiable property", under the Act, embraces not only physical property which can be specifically identified as belonging to the claimant, but also property, including cash, which has been "allocated" to a customer on the filing date of the petition. The court stated that the fact that the brokerage had received funds from the sale of stock owned by the customer and had credited his account in the amount received justified a finding that the funds were allocated to the customer at the time when the bankruptcy petition was filed, and that the funds were therefore specifically identifiable property which the trustee was required to return to the customer. The court further stated that if the amount in the customer's credit balance should not be considered to be specifically identifiable property, then it constituted "net equity" in the customer's account (see § 19 , infra).

It was held that margin customers of a bankrupt broker were not entitled to pay the amounts owing on securities purchased on margin and previously held by the broker, and to receive the proceeds of sales of those securities which had been effected by the trustee, in *Securities & Exchange Com. v Albert & Maguire Secur. Co. (1974, DC Pa) 378 F Supp 906*, the court concluding that such securities were not specifically identifiable property within the meaning of the SIPA. The securities had been pledged by the broker as collateral for a loan, and upon initiation of liquidation proceedings, the trustee sold the securities and discharged the loan with the proceeds. Pointing out that the securities were in the name of the pledgee and in its possession, the court stated that they were not individually segregated and could not have been, because they were not in the customers' names nor otherwise identified as belonging to them. The court also stated that the securities were not specifically identifiable property, by reason of bulk segregation, since bulk segregation refers only to securities which have been received or acquired for the accounts of customers who have an immediate right to receive such securities from the broker. The court stated that securities for which a broker has paid a portion of the purchase price, or has lent cash or securities to a customer, are not commonly regarded as entitling the customer to immediate possession and are therefore not required to be segregated, but may, in accordance with usage and custom, be pledged by the debtor. Since the securities in question were not fully paid for, the court concluded that the customers were not entitled to immediate possession, and that the securities were therefore not specifically identifiable as having been segregated in bulk for customers collectively.

Trustee appointed pursuant to liquidation proceeding under Securities Investor Protection Act is required to return specifically identifiable property to customers entitled thereto and to distribute single and separate fund; to be specifically identifiable property, under Securities Investor Protection Act, security must have remained in its identical form and have been in possession of brokerage firm on filing date, or have been allocated to or physically set aside for customers of brokerage on that date; required "bulk segregation" pertains to securities which have been received or acquired for accounts of customers who have immediate right to receive those securities from broker. *Securities & Exchange Com. v Investors Security Corp. (DC Pa) 415 F Supp 745*, affd in part and vacated in part on other grounds (CA3) *560 F2d 561.*

Money held by trustee, derived from stock lending transactions with creditor, was property of estate in liquidation

proceeding under Securities Investor Protection Act (SIPA), although books and records of debtor identified particular amounts of cash collateral posted by creditor to debtor; debtor was not required to segregate any cash for benefit of creditor, and debtor exercised its rights of alienability under parties' master securities loan agreement (MSLA), and thus, creditor could not trace and identify particular assets in possession of trustee. Bankr. Code, *11 U.S.C.A. § 541;* Securities Investor Protection Act of 1970, §§ 1(a) et seq., *15 U.S.C.A. §§ 78aaa* et seq.; N.Y. McKinney's Uniform Commercial Code §§ 9–207, 9–625. *In re MJK Clearing, Inc., 286 B.R. 109 (Bankr. D. Minn. 2002).*

Trustee under Securities Investor Protection Act is required by § 6(g) of Act *(15 U.S.C.A. § 78fff*(g)) to satisfy promptly, up to statutory limits, customers' claims for specifically identifiable property or net equities by delivery of specifically identifiable securities or cash, or distribution of cash or securities out of single and separate fund, or cash payments derived from SIPC advances; Act is narrowly drawn and contemplates return of customer's property in traditional form of stocks, bonds, and cash, where stockbroker holds or should be holding such property in customer's account, rather than return of value of what might be termed property or property rights involved in carrying out investment contract which uses or trades in traditional forms of stocks, bonds or cash where broker is to exercise investment judgment and expertise in actual investment of such securities in risk–free production of financial return for customer. *Securities Investor Protection Corp. v Associated Underwriters, Inc. (DC Utah) 423 F Supp 168.*

[*C] Attorneys' and trustees' fees

[*22.] 5 Single and separate fund

Single and separate fund, under § 6(c)(2)(B) of Securities Investor Protection Act *(15 U.S.C.A. § 78fff*(c)(2)(B)), is not composed of assets of debtor, but rather, property of customers; trustee is charged with administering fund to provide maximum distribution to customers; if customer entitled to share in fund has cause of action against third party for same property, trustee should be entitled to take assignment of claim in order to avoid unnecessary drain on fund; trustee is not limited to standing in shoes of debtor. *Securities & Exchange Com. v Albert & Maguire Secur. Co. (CA3) 560 F2d 569.*

[*23] Fees for trustees and trustees' counsel
[*23a] Determination of reasonableness

In the following case, the court discussed factors to be taken into account in the determination of the reasonableness of a fee to be paid to a trustee and his counsel for services rendered in a liquidation proceeding under the SIPA.

See also *Securities Investor Protection Corp. v Charisma Secur. Corp. (1972, DC NY) 352 F Supp 302,* a proceeding relating to the request of a trustee and his counsel for interim fees, where the court, commenting generally on allowable fees under the SIPA, noted that the primary criterion was not rigid economy, as in straight bankruptcy, but the striking of a reasonable mean between the two extremes of free choice and forced economy in determining what constitutes reasonable compensation. The court stated that some of the factors to be considered were whether professionals or paraprofessionals might be utilized for the services needed, whether the bulk of the work would require the service of accountants rather than lawyers, and whether the work required was legal or clerical in nature. Noting that the trustee and counsel had valued their time at rates said to be fair and reasonable under "present day economics in the practice of law in New York City," the court stated that while it was not limited by the economical spirit of the Bankruptcy Act, as it would be in an ordinary bankruptcy proceeding, neither was the court obliged to adopt the prevailing fee schedule among "going rate" firms in the New York legal communities, for the conduct of private litigation.

Where, subsequent to a liquidation pursuant to the provisions of the SIPA, the trustee and his counsel applied to the court for fees in the amounts of $5,000 and $25,000, respectively, the court in *Securities Investor Protection Corp. v Charisma Secur. Corp. (1974, DC NY) 371 F Supp 894,* affd (CA2 NY) *CCH Fed Secur L Rep P 94878,* pointed out that the liquidation had been a simple one, involving few legal problems, and directed fees to be paid in the amounts of $3,500 and $6,500, respectively. The court noted that the work involved was primarily of an accounting nature, that the accountants had in fact performed most of the services in the liquidation, and that the accountants had been paid approximately $14,000, substantially less than the fees requested by the trustee and attorney. The court also noted that one of the few areas of legal work performed related to litigation in which the trustee brought a securities fraud suit against a former principal of the debtor, the court pointing out that such suit was not authorized by the court before it was filed, nor allowed to proceed once the court ascertained that at best there was a speculative basis for the claim and a dim probability of collection for the estate, even if brought to judgment. The court noted that the SIPA required that liquidations be conducted in accordance with, and as though they were proceeding under, Chapter X of the Bankruptcy Act, and stated that while the "economical spirit" of the Bankruptcy Act did not limit the allowance of fees in a SIPC

liquidation, the court's function was to allow reasonable compensation for such expert legal and administrative work as was reasonably and sensibly required by the circumstances presented, and in fixing the proper fee, to strike a reasonable mean between the two extremes of free choice and forced economy. The court commented that the trustee and his counsel were entrusted with the highest standards of diligence and responsibility, and that the brokerage community, which finances the fund, was entitled to no less than such in the treatment of its contributions. The court pointed to the fact that the applications for fees referred to many hours of extensive research into the background of the securities industry, but the court stated that such time must be discounted, since it was neither the function nor the purpose of the SIPA to compensate lawyers, altogether unfamiliar with the field or with the securities business, for such self–education. The court stated that although it had no function in the selection of a trustee or its counsel, the court was entitled to presume that the SIPC appointed and recommended attorneys selected for their acquaintance with, if not their expertise in, that area, the court concluding that it would be inappropriate to compensate selectees for acquiring basic background knowledge which undoubtedly was presumed in making their initial selection. Also, the court noted that the fees requested represented, in part, work done prior to the appointment of the trustee and counsel, the court stating that it would not be proper to allow compensation for work done in a liquidation that had not yet been ordered to be commenced, or before the applicants were employed and authorized by the court to act. Moreover, the court held that it was not bound by the fact that the SIPC had approved the fees requested by the trustee and the trustee's counsel. Questioning the extent to which the SIPC had examined the claims prior to indicating its approval, the court stated that the SIPC's support of the full fees added no weight under the circumstances. In addition, the court noted that if the requested fees were paid, they, in conjunction with the accounting fees of approximately $14,000 which already had been paid, would slightly exceed the total amounts paid out to claimants in the liquidation. Furthermore, the court, noting that the trustee and his counsel, in requesting fees for their services, attempted to bill their time at the "going rates" for law firms in New York, stated that such "going rate" was not necessarily the standard for determining allowances in a simple, routine liquidation which involved little more than accounting ascertainment and payment of net equities of stock brokerage customers. In affirming the District Court's decision, the Court of Appeals commented that the District Court was required to scrutinize the reasonableness of the fees and that the fact that the SIPC was paying the fees would not justify the court's disregarding the need for a sensible and economic administration.

In liquidation of securities brokerage firm under Securities Investor Protection Act, bankruptcy court has authority to authorize administrative expenses to be allocated between general estate, which is for benefit of creditors of insolvent broker–dealer, and single and separate fund, which is for benefit of broker–dealer's customers. *Re Weis Secur., Inc. (DC NY) 416 F Supp 861.*

Fee requested by trustee and counsel, with respect to liquidation proceedings under Securities Investor Protection Act, of approximately $150,000 was excessive where liquidation was not involved and complicated, only 186 customers and 30 broker–dealers filed claims, and only 6 claimants objected to trustee's determination, and where trustee had assistance of accounting firm which, among its other activities, reviewed every claim that was filed and, for their services, received approximately $27,000; appropriate fee for trustee and counsel was $90,000. *Securities & Exchange Com. v Kelly, Andrews & Bradley, Inc. (DC NY) 423 F Supp 645.*

Fact that Securities Investor Protection Corporation, which ultimately will pay fees to trustee and trustee's counsel, acquiesces in requested fees does not relieve court of its responsibility for exercise of independent judgment on that issue; considerations of public policy require that courts be vigilant to prevent imposition of excessive fees upon fund out of which payment is made and which is derived from assessments upon financial community. *Securities & Exchange Com. v G. M. Stanley & Co. (DC NY) 424 F Supp 1352.*

As in Chapter X reorganizations and unlike straight bankruptcies, rigid economy is not primary criterion for fee allowances in SIPC liquidations; court must be careful to avoid permitting brokerage liquidations to be turned into opportunity for vicarious genorosity at expense of stricken entity, or of brokerage community which supports SIPC; only services requiring legal expertise are compensable by award of counsel's fees, so that even if hours devoted to non–legal matters by firm personnel were prudent expenditure of time, they may only be reimbursed at cost; enumeration of hours spent on clerical and administerial services is essential; fee application of law firm of which trustee is partner must carefully segregate services rendered, lest trustee be permitted to profit from non–legal services to estate in violation of his fiduciary duties. *Securities & Exchange Com. v Kenneth Bove & Co. (SD NY) 451 F Supp 355.*

[*23b] Interim fees

In the following case, the court, declining to award interim fees to the trustee and his counsel in a liquidation

proceeding under the SIPA, stated that the proper time to determine the amount of such fees ordinarily is at the completion of the administration of the estate involved.

In *Securities Investor Protection Corp. v Charisma Secur. Corp. (1972, DC NY) 352 F Supp 302,* an action involving an application for an interim fee allowance to the trustee and the counsel for the trustee serving in the liquidation of a brokerage business pursuant to the SIPA, the court declared that the determination of the amount of compensation to be paid for such services should ordinarily be deferred until the practical completion of the administration of the estate involved, and that interim allowances should be an exception and not the rule. The conclusion of an SIPC proceeding and of the delivery of securities and cash to the customers is the time when the court is best able to evaluate the overall requirements and results of the proceeding and the applicant's contribution thereto, emphasized the court. The court stated that until such time, no fair estimate of the overall contribution of the services is feasible in the ordinary case.

[*24] Attorneys' fees other than for trustees' counsel

[*24a] Fees for debtors' attorneys

Where counsel for a broker–dealer sought payment of his legal fees from the estate of the dealer or from SIPC funds, the court, in the following case, found that the provisions of *15 U.S.C.A. § 78fff*(f)(2) provided no basis for the making of such payments.

Where attorneys for a registered broker–dealer sought payment of, legal fees for their services in resisting the application of the SIPC for appointment of a trustee to liquidate the business of the broker–dealer, as a matter of first priority from the estate of the dealer, or from SIPC funds, or from both, the court, in *Securities & Exchange Com. v Alan F. Hughes, Inc. (1973, CA2 NY) 481 F2d 401,* cert den *414 US 1092, 38 L Ed 2d 549, 94 S Ct 722,* rejected the argument that the SIPA and the Bankruptcy Act authorized the compensation, and affirmed the denial of the application for such fees. The attorneys argued that under *15 U.S.C.A. § 78fff*(f)(2), the SIPC, in addition to advancing funds for claims of customers against the broker–dealer being liquidated, may advance to the trustees such moneys as may be required to effectuate the powers of a trustee under the Act, including the power to hire and fix the compensation of all personnel who are deemed by the trustee necessary for all or any purposes of the liquidation proceeding. The attorneys asserted that since the court had held in a prior opinion that a de novo judicial hearing was an integral aspect of an SIPA liquidation proceeding, one of the "purposes" of that proceeding must be to give a broker–dealer a chance to show that the claims against it are insufficient or incorrect, and that, therefore, the SIPA authorizes compensation for legal services in that endeavor. Rejecting this argument, the court stated that the Act made it clear that the purposes of liquidation proceedings were to return specifically identifiable property to the debtor's customers, to pay customers, to operate the debtor's business in order to complete open contractual commitments, to enforce rights of subrogation, and to liquidate the debtor's business. The court concluded that the legal services in question did not fit into any of those categories, and that while the attorneys' argument, in its simplest form, was that resisting liquidation is a purpose of the liquidation proceeding, Congress did not so provide. (For a discussion of the constitutionality of interpreting the SIPA so as not to provide for the payment of the broker–dealer's attorneys' fees for services provided in resisting liquidation proceedings, see § 4 , supra.)

[*24b] Fees for claimants' attorneys

In the following case, it was held that a claimant's attorney, who had successfully appealed the disallowance of his client's claim in an SIPA liquidation, had the right to payment of his fees out of the liquidation estate on the ground that his activities had benefited the estate through causing valid claims to be paid, it being pointed out that under § 243 of Chapter X of the Bankruptcy Act *(11 U.S.C.A. § 643),* incorporated in the SIPA through § 6(c)(1) of the Act *(15 U.S.C.A. § 78fff*(c)(1)), a court may award attorneys fees for services which were beneficial to the administration of the estate.

Section 243 of Chapter X of Bankruptcy Act *(11 U.S.C.A. § 643)* is not applicable to proceedings under Securities Investor Protection Act and claimant's attorney's fees cannot be awarded in SIPA liquidation on basis of § 243. *Securities & Exchange Com. v Aberdeen Secur. Co. (CA3) 526 F2d 603.*

It was held that a claimant's attorney, who had successfully prosecuted the claimant's right to payment under the SIPA, was entitled to be compensated out of estate funds, in *Securities & Exchange Com. v Aberdeen Secur. Co. (1974, DC Del) 381 F Supp 614,* on the ground that the attorney's activities had benefited the estate. The claim of the attorney's client initially had been disallowed, whereupon the attorney appealed, with the ultimate result that his client's claim, as well as that of others in similar positions, was recognized as being valid. Pointing out that under the applicable provisions of § 243 of Chapter X of the Bankruptcy Act *(11 U.S.C.A. § 643),* incorporated in the SIPA under § 6(c)(1) of the Act *(15 U.S.C.A. § 78fff*(c)(1)), a court may award compensation and expense reimbursement to an attorney for services which

were beneficial in the administration of the estate, the court stated that if the attorney had not taken the appeal on behalf of his client, the liquidation would have been carried out without the trustee recognizing the rights of the attorney's client and similar claimants, contrary to their entitlement under the law. The court concluded that compensation was due, since it was of benefit to the estate administration to have the law adhered to rather than violated. Accordingly, the court awarded to the attorney a fee, based upon the usual hourly rates of his firm, for the time he spent in actual preparation and conduct of his activities which led to the recognition of valid claims. The court deleted, however, such portions of the attorney's claim as related to time spent in the unsuccessful prosecution of different issues, and in furtherance of the claims of other clients.

FOOTNOTES

n1 P. L. 91–598 § 1(b), 84 Stat 1637, provided that headings for sections and subsections, and the table of contents, are included only for convenience, and shall be given no legal effect.

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