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NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC., 1707 H ST., N.W., WASHINGTON, D. C.

43 CASES DECIDED BY BOARD OF GOVERNORS

On September 24-26, the Board of Governors of the NASD held its annual Fall meeting.

To give readers of the NEWS a brief account of what took place at the meeting, listed below are short descriptions of the major points of interest discussed and actions taken by the Board.

- Considered 43 Business Conduct cases appealed to or on review by the Board since the May meeting. This was the largest number of cases ever presented at a Board of Governors' meeting.

- Approved holding an additional Board meeting in December to lighten the load of business conduct matters to be considered at the January, 1963 meeting, and allow for more time to discuss policy matters.

- Appointed a nominating committee which will present in December the names to be considered for Chairman and officers of the Association for the year 1963.

- Voted approval of new accidental death and dismemberment insurance plan to be offered voluntarily to employees of NASD members at rates 30 to 65% below comparable individual policies.

- Discussed and approved the development of an NASD Employee Handbook outlining Association policy and standards of conduct for the staff.

(Continued on Page 2)

NASD MEMBER FINANCIAL REPORTS SHOW 113 NET CAPITAL RULE DEFICIENCIES

One hundred thirteen apparent capital rule deficiencies have been determined as a result of a careful analysis of more than 4600 financial statements submitted by members in compliance with an Association request of July 10.

A special staff of six examiners reviewed the financial reports to determine whether the member was in compliance with the SEC's Net Capital Rule 15c3-1, which limits the ratio of "aggregate indebtedness" to "net capital" as these terms are defined in the rule. All cases in which it appeared that members were not in compliance have been referred to the SEC and the appropriate NASD District Committee, including one case which was an apparent insolvency.

In some cases, the net capital deficiency was corrected a few days after the statement was submitted, while in a number of other instances additional information was requested from firms to permit judgment as to their capital position.

A preliminary breakdown of the reported deficiencies indicates that approximately 40% were caused by an excess of liabilities over liquid assets; 45% were caused by the "haircut" which is the percentage deduction given the firm inventory to allow for fluctuations in market value, and 15% had some capital after the "haircut" but not enough to meet the requirement.

Although the NASD does not require the submission of an annual financial report, all members of the Association are required by Rule X-17a-5 of the SEC to submit such statements to the Commission.

The Commission's Rule requires, among other things, that the financial reports be filed with the SEC as of a date in each calendar year and within 45 days of that date. Members are cautioned that failure to file a timely report with the SEC constitutes a violation which not only makes the member subject to SEC sanction, but also to the possibility of disciplinary action by the NASD.

In commenting on the Association's program relating to the above matters, Executive Director Wallace H. Fulton pointed out that failure to submit reports to the NASD when requested, failure to meet the SEC net capital requirements or failure to make adequate and timely filings of the Form X-17A-5 report to the Commission, are serious violations of Association rules, as well as those of the SEC, not merely technical infractions.

SEC ASKS SMALL FIRMS FOR FINANCIAL DATA

The SEC has mailed questionnaires to 1200 small concerns who were exempt under the "two million dollar standard" from filing periodic financial reports after a public stock offering. The Commission wants to know what changes, if any, have taken place in the companies' financial structure since filing the original prospectus or Regulation "A" offering circular. Information from the questionnaires was required to be returned by October 1.

BOARD MEETING
(Continued from Page 1)

- Discussed at length a proposed SEC rule aimed at restricting boiler shop operations and prepared a statement to be presented to the Commission containing the reactions of the Board on various sections of the proposed rule.

- Approved a resolution authorizing newly elected District Committee members to take office on January 15 instead of March 30.

- Voted to raise again the passing score on the qualification examination given to registered representatives, effective November 1, 1962.

- Discussed a draft of revisions to the By-Laws, interpretations and resolutions, Rules of Fair Practice and Code of Procedure.

SIX EXAMINER TRAINEES ADDED TO NASD STAFF AT WORK ON SIX-WEEK INSTRUCTION COURSE

Seated around a conference table in the Executive Office are six new examiner trainees, recently employed by the Association, who are participating in an intensive six-week classroom course before continuing their training in assigned district offices. Directors of the course, Ray Moulden, Secretary of the Investment Company Committee, and Edward Gilleran, Chief of Examiners, are explaining details of a balance sheet to the new examiners.

COMPTROLLER MAY TRY TO LIBERALIZE PROMOTION OF BANK COMMON TRUSTS AS CONGRESS SWITCHES CONTROL

In announcing the appointment of five trust bankers to act as technical advisors for reviewing existing common trust regulations, Comptroller of the Currency James J. Saxon said that present rules place unnecessary limitations on the banks administering these arrangements and prevent some segments of the public from enjoying the advantages that common trusts offer.

Just recently, President Kennedy signed a bill which transfers authority to regulate bank common trusts from the Federal Reserve System to the Comptroller's office (see story on Page 3) at a time when the Federal Reserve Board was considering an amendment to Regulation "F" which would have tightened rather than liberalized its rules concerning these trusts. At the end of 1961 there were 511 common trusts operated by 327 banks across the country.

Early in 1961, the NASD and the Investmant Company Institute filed a joint position statement with the Federal Reserve Board in support of an amendment to Regulation "F" which would further restrict banks from offering these trust agreements to small investors through active merchandising campaigns. The NASD and the ICI presented evidence citing numerous examples of banks which were advertising in newspapers and promoting in booklets the fact that investors could purchase securities by setting up a trust agreement whereby moneys would be pooled by the bank to assemble various types of investment objective portfolios which would be constantly supervised by trust officers.

In their position statement to the FRB, the NASD and the ICI pointed out that it was never the intention or spirit of Regulation "F" to allow banks to operate a mutual fund type of business through common trust agreements which were not registered with the SEC or subject to the regulations of the 1940 Investment Company Act.

Regulation "F" says that common trust agreements may be created only to allow banks to act in a fiduciary capacity in administering more effectively and economically certain accounts for which they hold appointments as trustee, executor, administrator or guardian. The regulation prohibits the operation of such common trusts for other than these strictly fiduciary purposes.

The NASD and the ICI further stated in their brief that if banks actively merchandise common trust facilities, such trusts would not only assume the characteristics of a mutual fund but the trust instrument the customers sign could in essence be construed as a security subject to registration with the SEC under the 1933 Securities Act.

Since filing the joint brief, the Association has discovered several additional examples of banks (one recently in Texas) engaging in actively promoting common trusts to the general public. All of these instances have been brought to the attention of the Comptroller's office.

NASD SPEAKERS' GUIDE BEING DEVELOPED TO HELP MEMBERS IN THEIR LOCAL PROGRAMS

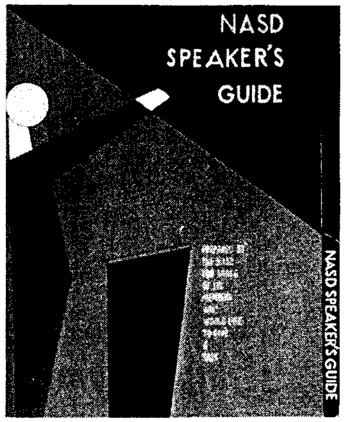
The NASD staff is now preparing a comprehensive Speakers' Guide, expected to be completed by the end of the year, which will be helpful to members and registered representatives in establishing local level speaking schedules and programs.

Pictured at right is the rough layout of the folder-type kit which will contain significant topic headings on various aspects of the securities business. Under each heading will be a concise, factual approach to the topic as well as additional reference material which will put research facts concerning the subject at the user's fingertips.

In preparing a talk, the NASD member or registered representative may combine one, two or more topic sheets to develop a complete speech.

Also included in the kit will be a section devoted to acquiring speaking engagements and merchandising this type of opportunity for the benefit of the firm and the individual.

The NASD Speakers' Guide will



contain a list of service clubs and civic groups which would be receptive to scheduling a speaker, a list of give-away literature from the NASD and other securities business organizations, sample news release and publicity ideas, an outline for establishing a local speakers' bureau and sample advertisements which can be used by those who wish to initiate a discussion group or investment class as part of their public relations program.

From time to time, after the publication of the NASD Speakers' Guide, additional inserts will be developed to increase further the effectiveness of this material.

NEW SELLING SCHEME LEADS TO EXPULSION

An unusual selling scheme was uncovered in a recent expulsion decision appealed to the Board of Governors involving 117 consecutive transactions where mark-ups ranged from 10% to 100%.

In this case, a great majority of the respondent's business resulted from advertisements placed in newspapers directed at servicemen which offered information on specific low price, obscure issues. When a customer answered an ad, he was sent literature on those securities in which the firm always held a position, together with an order form containing the name and price of the issue, a space for noting the number of shares desired and a line which read, "I enclose $.......... in full payment".

When the orders were received by the firm, a confirmation was sent to the customer which invariably stated, "Your check in the amount $.......... has been received. We are billing you at the current market of $........... Please forward your check to cover the balance."

The member admitted that the firm offered to sell securities at prices printed on the order blank and that, in many instances, the price quoted on the confirmation was unrelated to the current market. But he maintained that a notation placed unobtrusively at the bottom of the order form stating "Prices subject to change" was sufficient to let customers know that the stated prices were not firm.

The Board upheld the District Committee findings in the case that the order form was misleading and confirmed prices were unrelated to the current market, as well as other findings of net capital violations, failure to register a representative, failure to maintain proper books and records, granting selling concessions to a non-member and failure to supervise transactions of employees. The penalty of expulsion and assessment of costs was upheld by the Board.

BANKERS' ADVISORY GROUP RECOMMENDS TRANSFERRING REG "T" AND "U" TO TREASURY

A special advisory committee of bankers, appointed by James J. Saxon, Comptroller of the Currency, has recommended to President Kennedy some sweeping changes in the National Banking System, one of which was the transfer of supervision of Reguation "T" and Regulation "U" from the Federal Reserve Board to the Treasury. Regulation "T" deals with the extension of credit by broker/dealers and Regulation "U" concerns loans by banks for buying and carrying securities.

In a companion move, President Kennedy signed a bill on September 30 transferring authority to regulate all common trusts from the Federal Reserve System to the Comptroller of the Currency. (See story on Page 2.)

Meanwhile, the Federal Reserve Board has sent questionnaires to 500 banks requesting information on stock secured loans to customers for purchase of other stocks not listed on a national securities exchange. Such loans are not currently covered by Regulation "U". According to the FRB, information obtained from these questionnaires will be passed on to the SEC Special Study Group to aid in making recommendations to Congress concerning tightening present laws on stock loan practices.

LOCAL NASD MEETINGS HELP INFORM MEMBERS

A number of District Committees have reported the successful completion of a series of NASD membership meetings in various cities in their respective territories. Other meetings have been scheduled for the future in almost all Districts.

Recent conferences held in Phoenix, Denver, Salt Lake City, Tulsa, Omaha, Albuquerque, Oklahoma City, Wichita, Kansas City, St. Louis and Birmingham have each drawn an average attendance of 70 to 100 officers and registered representatives from member firms.

The gatherings have been specifically designed to cultivate an exchange of ideas and information about the operations of the NASD and usually include presentations by the District Secretary and District Chairmen or Board member, followed by an informal question and answer period.

A welcome reaction in the meetings held so far this year has been an increased awareness of the Association's many activities and programs beyond its responsibilities in the regulatory field, and a marked change from the sometime attitude that the NASD is little more than a paid policeman.

At these meetings there was also considerable interest expressed in learning more about other activities such as the gathering and publishing of over-the-counter quotations; the work of the Uniform Practice Committee in formulating guidelines for the business; the creation of the National OTC Clearing House; the examination program and the development of a new study guide.

It was pointed out at several of the meetings that one of the major benefits of NASD membership is the opportunity for the broker/dealer community to express its views and present suggestions through the Association on pending SEC rules and legislation proposed to Congress.

SEC BACKS NASD IN REQUIRING CAREFUL CHECK OF EMPLOYEE CHARACTER

On August 8, 1962, the SEC sustained the NASD's Board of Governors in its expulsion of Vickers, Christy & Co., Inc. and in the revocation of the registrations of Sidney L. Vickers, Jr., and William J. Christy for improperly certifying the good character of registered representatives without adequately investigating the background of these employees.

This decision, plus a wealth of testimony at the SEC's public hearings on qualification and training of salesmen, points up the desirability of reminding members of their obligations under Article III, Section 27 of the Rules of Fair Practice.

The Commission found that Vickers, Christy and its principals had violated Article III, Section 1 and 27(c) of the Rules of Fair Practice by certifying on the registration application of four salesmen that the firm had reason to believe the people in question were of good character and good business repute.

In its decision, the Commission stated that casual interviews and perfunctory telephone calls to a former employer did not constitute a reasonable investigation of an applicant's character. The use of the phrase, "I HAVE COMMUNICATED WITH THE APPLICANT'S LATEST EMPLOYER", on the NASD application form does not reduce the obligation imposed by Section 27, according to the Commission, and the fact that the NASD did not reject the registration does not nullify the plain terms of the Section. The complete responsibility of the investigation, as the Section points out, is upon the member.

The SEC decison stated in part, "Both the NASD and the Commission have been concerned with raising the standards of character, competence, and training of securities salesmen. This basic obligation, implemented by the NASD in their adoption of Section 27, is appropriate in the public interest. We cannot find that the penalties imposed by the NASD for such reckless hiring procedures were excessive or oppressive in light of the member's duty under the rule."

MEMBERS NEED CUSTOMER NUMBERS

In connection with a new Federal law requiring the use of tax-payer identifying numbers on interest and dividend documents that broker/dealers must file with the Internal Revenue Service, NASD members should begin in the immediate future to ask all customer accounts for this information. Customer account numbers must be used on all documents covering payments made on or after October 1, 1963.

The term "customer account number" means either the customer's Social Security number or an identifying number assigned by the Internal Revenue Service to those tax payers who don't have a Social Security number.

The IRS suggests the following language be used in obtaining required information from customers:

"As you may have already learned, new Federal law requires the use of taxpayer identifying numbers on Federal tax returns, effective for the tax year 1962 and thereafter. The same law requires you to furnish us your number and that we include it with your name and address on documents we must file with the Internal Revenue Service. If you have a Social Security number, it willl also be your tax account identifying number. To comply with the law, please indicate your Social Security number, if you have one, in the space provided. If you do not have a Social Security number or cannot locate your number, do not take any action toward obtaining a number as a result of this letter. The Internal Revenue Service has a program for assisting persons needing numbers and you will be advised how to proceed."