NASD News

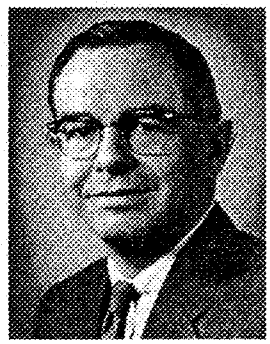
VOLUME XXIII, NO. 1 APRIL 1963

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

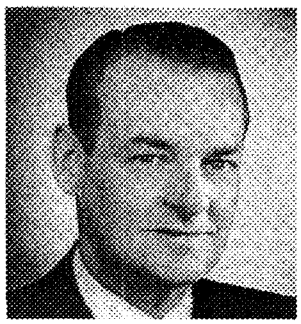
MERRILL COHEN NAMED NASD BOARD CHAIRMAN FOR 1963
OTHER OFFICERS LEMKAU, McHENRY, FLEMING AND FULTON

Merrill M. Cohen
J. M. Dain & Co., Inc.
Minneapolis
Chairman 1963

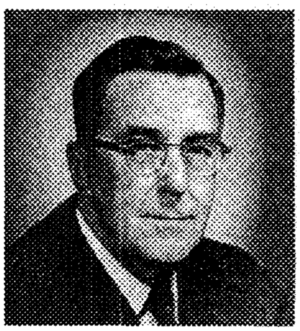
Hudson B. Lemkau
Morgan Stanley & Co.
New York
Vice Chairman 1963



Merl McHenry
J. Barth & Co.
San Francisco
Vice Chairman 1963



Robert W. Fleming
Folger, Nolan, Fleming & Co., Inc.
Washington, D. C.
Treasurer 1963



Wallace H. Fulton
Executive Director

Merrill M. Cohen, president of the Minneapolis securities firm of J. M. Dain & Co., Inc., was named the 1963 Chairman of the Board of Governors at the Board's January meeting. Mr. Cohen succeeds Avery Rockefeller, Jr., partner, Dominick & Dominick, New York, as head of the 21-man group.

Other officers elected by the NASD Board were: Vice-Chairmen, Hudson B. Lemkau, a partner in Morgan Stanley & Co., New York, and Merl McHenry, a partner in J. Barth & Co., San Francisco; Treasurer, Robert W. Fleming, Executive Vice-President of Folger, Nolan, Fleming & Co., Inc., Washington, D. C., and Wallace H. Fulton, Washington, D. C., to continue as Executive Director.

A member of the NASD's Board of Governors since 1961, Mr. Cohen served in 1962 as a Chairman of the National Business Conduct Committee. He is a former governor and vice chairman of the Midwest Stock Exchange.

Following his education in Minneapolis public schools, Mr. Cohen began his business career in 1918 with the Minnesota Loan & Trust Co., in Minneapolis. He was with

(Continued on Page 2)

WALLACE H. FULTON RETIRING AS NASD CHIEF EXECUTIVE

Wallace H. Fulton, NASD's Executive Director for the past 24 years, has announced his intention to retire a year from now, on April 1, 1964. The retirement will come two weeks after his 68th birthday.

Mr. Fulton has served the Association since its organization in 1939 and prior to that was one of the leaders in establishing the concept and principles of self-regulation in the securities business that evolved through the Maloney Act from the Investment Bankers Code Committee and the Investment Bankers Conference Inc., the immediate predecessors of the NASD. Mr. Fulton was Director of Compliance of the Code Committee and headed the Investment Bankers Conference Inc. in the '30's. He has agreed to serve as a senior advisor to the 21-man Board of Governors after he retires.

Mr. Fulton's successor has not been chosen.

OTC CLEARING CORPORATION TO SHARE AMERICAN STOCK EXCHANGE FACILITIES

Kirvin

The National OTC Clearing Corporation has announced plans under which clearing facilities for approximately 1200 over-the-counter stock issues would be furnished by the American Stock Exchange Clearing Corporation on a service basis.

Exchange President Edwin D. Etherington and OTC Clearing Corporation President John H. Kirvin declared that the joint program calls for a pilot operation to be started this summer for approximately 100 issues. The entire program is expected to be running by late 1963.

The National OTC Clearing Corporation was established December 4, 1961, to provide members of the National Association of Securities Dealers, Inc., banks and others participating in the over-the-counter market with clearing facilities similar to those enjoyed by stock exchange member firm brokers.

Etherington and Kirvin said a six months study has shown that the Exchange Clearing Corporation's experience, personnel and data processing equipment can be effectively used by the over-the-counter clearing facility. They added that American Stock Exchange members who also do an over-the-counter business will be able to speed settlements and lower back-office costs.

The dual operation also will provide both the OTC Clearing Corporation and the Exchange Clearing Corporation with back-up equipment and manpower during heavy volume periods.

The OTC Clearing Corporation staff under the direction of Executive Vice-President Charles Gilroy, will work in conjunction with the staff of the Exchange clearing organization headed by August Gunther, Vice-President and General Manager. In the selection of OTC stocks to be cleared in the new system, a prime factor will be the trading volume in the New York market. However, availability of information with respect to the issuer and other factors will also be considered by the National OTC Clearing Corporation.

Early in 1962, the Exchange's Clearing Corporation moved from the Exchange Building into larger quarters at 12 Albany Street where a working area of 11,000 feet is available.

Under the joint program, over-the-counter transactions would be matched and off set, payments of net balances would be made and received, and deliveries would be allotted. These steps will minimize the handling of securities. The Exchange Clearing Corporation will be reimbursed on a reasonable basis for space, equipment and personnel as well as for out-of-pocket expenses. A contract covering the new arrangement is presently being prepared.

The first annual stockholders meeting of the National OTC Clearing Corporation was held on March 19, 1963, for the purpose of electing officers and directors for the coming year.

Directors chosen at the meeting were Board Chairman, Carl Stolle, President of G. A. Saxton & Co., Inc.; President of the Corporation, John H. Kirvin, Vice-President of Glore, Forgan & Co.; Alfred B. Averell, General Partner of Bache & Co.; Albert J. Eisenberg, General Partner of Sutro Bros. & Co.; Thomas MacDonald, Vice-President of Blyth & Co., Inc.; Kenneth W. Martin, Vice-President of Merrill Lynch, Pierce, Fenner & Smith, Inc.; William R. Muller, Assistant Vice-

(Continued on Page 6)

OFFICERS

(Continued from Page 1)

Forman State National Bank, Chicago, from 1929 to 1931, and with Piper, Jaffray & Hopwood, Minneapolis, 1931 to 1935. He joined J. M. Dain in 1935 and has been president of the firm since that time. Mr. Cohen is a director of American Life Companies, Inc., American Premier Insurance Co., Buttrey Foods, Inc., Northwest Growth Fund, Inc., and Red Owl Stores, Inc.

LEMKAU

Mr. Lemkau was also elected to the Board in 1961 and has served as a member of the National Business Conduct Committee and the Executive Committee. Mr. Lemkau joined Morgan Stanley in 1942 and has been a partner since 1956. He lives in Plandome, New York, and has two sons and a daughter.

McHENRY

Merl McHenry also came on the NASD Board in 1961 and in 1962 served as a Chairman of the National Business Conduct Committee. Mr. McHenry became a partner in J. Barth & Co. in 1952 after serving as Vice President and Trust Officer of the Bank of America. He is now the partner in charge of research at J. Barth.

FLEMING

Mr. Fleming formerly served as Chairman of NASD's District 10 Committee. Mr. Fleming joined Folger, Nolan & Co. in 1948 and became a partner in 1950. In 1956, the name of the firm was changed to Folger, Nolan, Fleming-W. B. Hibbs & Co., Inc. and Mr. Fleming became Executive Vice President. The firm is now known as Folger, Nolan, Fleming & Co. Mr. Fleming previously worked for Pan American World Airways. He has a daughter and two sons.

Elected for the 24th time, NASD's Executive Director Wallace Fulton has announced his intention to retire after this year (see story on page 1).

HAUSSERMANN NAMED COMMITTEE CHAIRMAN

Arthur H. Haussermann, vice president, secretary and treasurer of Vance, Saunders & Company, Inc., Boston, underwriters of one of the largest groups of mutual funds, is the new chairman of the Investment Companies Committee of the Board of Governors. He succeeds Franklin R. Johnson, executive vice president of Colonial Distributors, Inc., also of Boston. Mr. Haussermann, a lawyer, is assistant to the president of Boston Funds and Canada General Fund.

NEW INSURANCE PLAN REACHES $200 MILLION

The Trustees of the NASD Insurance program have announced that the new Disability Income and Accidental Death & Dismemberment insurance plan reached $200,000,000 at the closing date, March 31, 1963.

During the Charter Enrollment Period beginning December 1, 1962, thousands of applications, representing more than $22 million a year in long-term Disability Income benefits were received and almost $200,000,000 of all-risk, 24-hour, Accidental Death & Dismemberment insurance was issued to members since the opening of the plan.

The Trustees will consider reopening the program later in the year.

SELLING FUNDS BY IMPENDING DIVIDENDS RESULTS IN STIFF FINE FROM BOARD

Charges of failure to comply with the SEC's Statement of Policy, using impending dividends as an inducement for mutual fund purchases, making unsuitable recommendations to customers, and neglecting to supervise the correspondence of salesmen have resulted in an increased fine of $2,000 and censure for an NASD member and fines for three of the member's registered representatives.

One salesman since has had his registration revoked for failure to pay the fine.

The Association charged that these branch office salesmen prepared and sent out to the public 79 separate sales letters that violated one or more sections of the Statement of Policy.

Also, on nine occasions these same letters contained such statements as:

> "I should recommend . . . that you let us place this $3000 investment prior to January 2, as dividends are being credited to stock as of record this date in one of the three funds . . . "
> "Here's an opportunity to pick up a quarterly dividend on an excellent investment. The current price is $11.32 (October 31st market close) and the dividend of 22¢ is an approximately 8% annual basis . . . "
> "If you had bought last week at $10.03 you would have your dividend covered even if it drops 17¢ after dividend date."

The NASD Board of Governors held on review that this practice of using impending dividends as an inducement for the purchase of investment company shares without also giving full explanation and disclosure as to the effect of the dividend or the distribution constituted conduct inconsistent with just and equitable principles of trade and thus violated Article III, Section 1 of the Rules of Fair Practice.

One of the registered representatives was found to have recommended to a customer the investment of $20,000 in three different balanced funds, and several months later recommended switching the customer's holdings to other funds, which resulted in $565 additional commissions. The Board found that the registered representative did not have reasonable grounds for believing that his recommendations were suitable in view of the financial condition and needs of the customer.

In defending the charge of failure to supervise, the member presented voluminous evidence, consisting of memoranda, news letters, booklets and other notices from the home office to new salesmen and branch offices, which called attention to the Statement of Policy and to rules of the NASD.

However, the Board could find no instance where the member ever reviewed the branch office correspondence file which disclosed the violations.

BANK TRUST RULE HIT BY INVESTMENT GROUP

The Investment Company Institute has challenged proposed rules of the Comptroller of the Currency, James A. Saxon, which give national banks the power to establish collective investment funds whereby moneys from investors could be pooled in such a fund for the purchase of securities.

The Investment Companies Committee of the NASD has filed a letter with Mr. Saxon's office supporting the ICI position.

The ICI in a brief sent to Saxon's office, challenged the entire concept of collective accounts, asserting that these new rules would exceed any authority granted the Treasury under the Glass-Steagall Banking Act.

PRUDENTIAL APPEALS SEC ANNUITY RULING

Variable annuity contracts proposed for offering to investors by Prudential Insurance Company of America are securities subject to SEC regulation, the Securities and Exchange Commission has ruled.

The insurance company has appealed the finding to the U. S. Circuit Court of Appeals at Philadelphia, and probably will seek U. S. Supreme Court review if the appeals court upholds the SEC.

The NASD had joined the SEC staff in opposing Prudential's plea that its variable annuity contracts are really a form of insurance not subject to Federal securities laws. NASD and the Commission staff argued that the variable annuity contracts in essence would be equity investments similar to the shares of investment companies and, therefore, their sale should be subject to the same Government regulations as mutual fund offerings.

The Commission, after hearings and oral argument, upheld the Association views by denying applications of Prudential for exemptions from the Investment Company Act. This action is similar to that taken by the Commission at behest of NASD in the case of Variable Annuity Life Insurance Company and Equity Annuity Life Insurance Company. These firms also appealed, the case reaching the Supreme Court which held in a precedent-making decision that variable annuity contracts are, in fact, securities subject to SEC regulation.

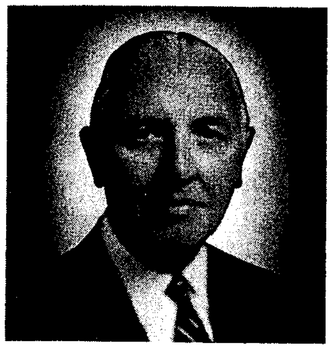
Variable annuity contracts involve an interest in a diversified portfolio of common stocks, the value of the contract fluctuating with the securities market. At maturity, the value of the account is the base from which a fixed percentage is paid annually to the annuitant as retirement income.

NEW MEMBERS OF NASD BOARD OF GOVERNORS

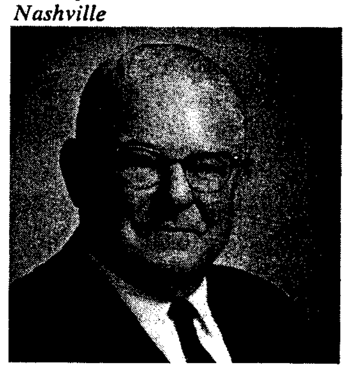
John W. Callaghan
Goldman, Sachs & Co.
New York

G. Shelby Friedrichs
Howard, Weil, Labouisse, Friedrichs and Co.
New Orleans

Gus G. Halliburton
Equitable Securities Corporation
Nashville



Joseph Ludin
Dillon, Read & Co., Inc.
New York

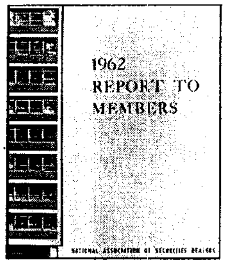


Malcolm F. Roberts
Hornblower & Weeks
Denver

Van S. Trefethen
Shuman, Agnew & Co.
San Francisco

Norman B. Ward, Jr.
Singer, Dean & Scribner
Pittsburgh

1962 ANNUAL REPORT HIGHLIGHTS TESTING AND NASD MEMBER EXAMINATION PROGRAM



The continuing responsibility of the securities business to provide better qualified and better trained sales personnel received major emphasis in the NASD's 1962 Annual Report to Members.

More than 2,200 new securities salesmen seeking to register last year with the Association failed the organization's qualification examination for registered representatives, according to the report.

Since the Association put its new and more difficult qualification examination into effect on January 1 last year, over 16,000 examinations were administered and in the last two months of 1962, the failure rate had risen to approximately 32%. In 1961, 30,790 examinations were given under the old NASD test procedure in which a pool of questions and answers were disclosed for study purposes. The failure rate under that system was approximately 3%.

Executive Director Wallace Fulton pointed out that Association examiners had inspected the books and records of more members and branches last year than in any previous year in the organization's history. Over 36% of the members and 14% of the branch offices were examined in 1962, compared with 31% of the members and 10% of the branches in 1961.

Complaints filed during the year resulted in the expulsion of 52 members and the revocation of 74 representatives. Other disciplinary action reported for 1962 included 15 members and 32 registered representatives suspended; 318 members and 64 registered representatives fined, and 332 members and 90 representatives censured.

Mr. Fulton stated that although Association membership for '62 had risen to an all time high of 4,771 firms, there was a marked decrease of more than 8,000 representatives registered by the Association, from the 102,000 figure recorded at the close of 1961. Registration of branch offices of member firms continued to increase to just over 4,700.

In his report to members, Avery Rockefeller, Jr., NASD's 1962 Board Chairman, called attention to the Securities and Exchange Commission's intensive special study of the securities markets. He said that through the study a magnifying glass has been held to the Association, its members and each of its present and future programs. Rockefeller warned that the expenses and direct cost involved in carrying out the Association's self-regulatory responsibilities would undoubtedly increase in the future. "The industry must be prepared," he said, "to finance the benefits allowed it under the Maloney Act."

The NASD's financial statement showed that income for 1962 was approximately $400,000 over income for the previous year; while expenses in 1962 exceeded 1961 by $383,733.

DON'T USE MAGAZINE "FUNDSCOPE," NASD MEMBERS WARNED

Dealers and salesmen are cautioned not to use the magazine "FundScope" for reference material or as sales literature in any effort to promote the sale of investment company shares.

It has come to the attention of the Investment Companies Committee that large numbers of subscriptions to this magazine are being ordered by some dealers and registered representatives. If any of these are being sent to members of the public, the practice should be stopped, the Committee warns.

(Continued on Page 6)

JOINT NASD, EXCHANGE QUALIFYING TEST SET

The NASD, New York Stock Exchange and American Stock Exchange will combine procedures for administering registered representatives' examinations in 63 centrally located NASD test centers throughout the United States beginning July 1.

The new arrangement is designed to provide more uniformity and convenience for member firms and candidates. It culminates three years of intra-industry effort to revise and coordinate examination systems into a single basic securities industry test, with special NASD, New York Stock Exchange and American Stock Exchange sections.

The new system will enable applicants seeking registration with firms that are members of the NASD and one or both of the exchanges to be examined at a single sitting in a convenient location. Under present procedures, applicants for registration with NASD firms take separate tests at NASD test centers in universities across the country. If their firms are New York Stock Exchange or American Stock Exchange members also, the applicants must take separate tests, sometimes in different cities.

Beginning July 1, candidates who seek to register only with the NASD will take the general and NASD sections of the test covering the Association's rules and questions common to all areas of the securities business. The general and NASD section will last two hours. Those also seeking to register with either the New York or American Exchange will take an appropriate additional section dealing with trading on the exchanges and their constitutions and rules. Each Exchange section will last about one hour.

(Continued on Page 6)

QUANTITY DISCOUNTS ON FUNDS CLARIFIED

Some questions have arisen as to who may be entitled to quantity discounts under Rule 22d-1 (Sections (a) through (e), inclusive) under the Investment Company Act of 1940 when purchasing shares of open-end investment companies for retirement plans.

The NASD Investment Companies Committee has prepared the following clarification:

Generally, Rule 22d-1 prohibits the grouping of funds of people or companies for the purpose of obtaining quantity discounts. The Rule does permit the giving of quantity discounts to a trustee or other fiduciary purchasing securities for a single trust estate or single fiduciary account, including a trust created under a plan qualified under Section 401 of the Internal Revenue Code, although more than one beneficiary is involved.

However, the granting of quantity discounts to any professional or trade association or trustee or other representative of such association administering a retirement plan for the benefit of the accounts of the association's individual members would be a violation of Rule 22d-1.

There follow several illustrative examples of purchases permissible or prohibited under Rule 22d-1:

Example 1

A number of doctors with separate practices belong to a medical society or other group. The society creates a retirement plan for all of these doctors and their employees, as permitted by the Keogh-Smathers Act. The purchase of shares of open-end investment companies by the retirement plan for this society *will not qualify* for quantity discounts under Rule 22d-1, since this is a group of individuals, or a group of individual trusts, whose funds are being combined in the purchase of such securities.

Example 2

A law firm decides to establish a retirement plan for the benefit of its partners and employees, as permitted by the Keogh-Smathers Act. Purchases of shares of open-end investment companies for the retirement plan established by this law firm, including amounts represented by contributions to the plan made by partners or employees, *would be entitled* to quantity discounts under Rule 22d-1, since the purchases are being made for a single fiduciary or trust estate, the beneficiaries of which are partners or employees of this law firm.

Example 3

A number of companies or self-employed individuals adopt separate retirement plans under a so-called master plan administered by a single trustee, permitted for purposes of convenience by the Internal Revenue Service. This trustee *may not* group the funds of the several plans for the purpose of obtaining quantity discounts under Rule 22d-1, since the purchases are being made for more than one trust estate.

TEST

(Continued from Page 5)

In the case of candidates seeking registration by both exchanges, the American Exchange will accept passing of the New York Stock Exchange section. Where a candidate's firm is a member of the American Exchange only, a test newly developed by that Exchange will be used.

The NASD's 63 testing centers will also be used for administration of qualification tests required for new members and allied members of the New York Exchange—that is, all new general partners and voting stockholders of member organizations.

"FUNDSCOPE"

(Continued from Page 5)

"FundScope" presents performance data on investment companies that is not in conformance with the SEC's Statement of Policy, the Committee states. It also has published articles that do not conform with the Statement of Policy standards for other aspects of investment companies and their shares. "FundScope," of course, is at liberty to publish any material it wishes and is under no obligation to conform with the Statement of Policy. Anyone selling investment company shares, however, the Committee points out, whether affiliated with an NASD member or not, must abide by the Statement of Policy in all representations to the public and is not permitted to send to or use with customers any published material that does not meet Statement of Policy standards.

CLEARING

(Continued from Page 2)

President of New York Hanseatic Corp.; John Weeden, Treasurer of Weeden & Co.; Irvin J. Whitehill, General Partner of Dean Witter & Co.

At the meeting, stockholders were told that as of February 11, there were 609 shares of common stock and 100 shares of limited participation voting stock outstanding. Under the provisions of the organization's certificate of incorporation, the limited participation voting stock, all of which is owned by the NASD, is entitled to elect two members of the Board of Governors and the common is entitled to elect the remaining members of the Board.