



To NASD Members and Registered Representatives:

**SALES REPRESENTATIVE
FINED BY NASD FOR
VIOLATING SEC RULES**

A sales representative of an NASD member was recently fined \$2,000 for improperly using sales literature which did not conform to the Securities and Exchange Commission's Statement of Policy.

The literature, which induced a number of customers to purchase mutual fund shares, described the advantages of mutual funds without warning about the inherent risks involved in this type of an investment and featured tables and charts that did not conform to prescribed standards. Other parts of the sales literature also violated a section of the Statement of Policy which prohibits material which is inaccurate in factual detail or creates a false or misleading impression as to any investment company's past performance or representations that the investor's experience will be repeated in the future.

The material in question was assembled by the representative without his employer's knowledge and was distributed without being submitted in advance to the NASD for approval.

**REGISTERED REPRESENTATIVE
EXAMINATION FORMS RECEIVE
OVERHAULING FROM NASD**

The Association has recently introduced new forms of the Qualification Examination for Registered Representatives which are now being used at NASD examination centers across the country.

The new forms are designed to better measure the extent of the preparedness of applicants and to disqualify those applicants whose training or understanding of the subject matter could in the past have been characterized as marginal.

The examinations are under continual review to insure high standards of qualifications for the entry of broker-dealers and their registrants into the securities business.

"Our industry is growing more complex every year," stated Richard Walbert, NASD president. "The Association realizes its responsibility to register only those applicants that have a thorough and current knowledge of the industry."

Applicants for registered representative are advised to use the most recent edition of the *NASD Training Guide*, issued in July, 1969, as a study manual.

**INDUSTRY LEGISLATION
RECENTLY INTRODUCED
BEFORE U. S. SENATE**

In early June, Senator Edmund Muskie (D.-Maine) introduced a bill (S. 2348) in the Senate which would establish a Federal Broker-Dealer Insurance Corporation, similar in purpose to the Federal Deposit Insurance Corporation, which insures bank and savings and loan customers.

The proposed FBDIC would guarantee that, in the case of a brokerage firm's being closed, that holders of insured customer accounts or insured liabilities would be reimbursed.

All brokers and dealers registered with the SEC would be insured under the proposed Act, and would be subject to its provisions.

Assessments of one-half of 1 percent per year multiplied by an amount equal to the net capital of a broker or dealer would be levied against each broker and each dealer by the Corporation.

Members of the SEC would comprise the Board of Directors of the Corporation which would be located in Washington, D.C.

Among the Corporation's powers would be to act as receiver, when necessary under law; to take steps to finalize a closed firm's business or to attempt to put the firm back on a sound financial footing; to audit all participating firm's books and otherwise examine all records for insurance and assessment purposes; and to impose penalties for failure to abide by its provisions.

Another Bill, S. 2742, proposed by Senator Eugene McCarthy (D.-Minnesota), would alter the current membership requirements on registered stock exchanges.

Under McCarthy's proposal, the only limitations to membership on a stock exchange would be registration by each broker or dealer with the SEC or a temporary limit with SEC approval, because of lack of floor space to accommodate additional members.

New exchange members, under the Bill, would have to pay a share of the value of the exchange's facilities to compensate members that already belong to the various exchanges.

McCarthy's bill was prompted by the fact that there are over 4,500 broker-dealers registered with the SEC, although there are only 1,366 seats on the New York Stock Exchange.

This proposed legislation would also open the door to other financial institutions' belonging to a stock exchange, thus enabling institutions to effect transactions without utilizing any brokerage firm.

Presently, mutual funds, insurance companies, and pension plans account for approximately half of the volume on the New York Stock Exchange.

The NASD is studying both bills to determine a position that will be responsive to the public and to the membership. Members will be advised of continuing developments regarding this legislation.

The Association's planned automated quotations system (NASDAQ) is moving smoothly toward its projected start up goal of late 1970.

The Bunker-Ramo Corporation's building in Trumbull, Connecticut, that will house NASDAQ's sophisticated computer complex is now under construction with completion expected soon. The first two 1108 Univac computers for the NASDAQ

**BUILDINGS, EQUIPMENT
NOW BEING READIED
FOR NASDAQ SYSTEM**

system will be delivered and installed early this fall. Programming for the NASDAQ system is already in progress.

To date 567 firms are under contract to subscribe to levels 2 and 3 of the system: 185 for Level 2 and 382 for Level 3.

Level 2 is designed for a broker-dealer with an order to execute and will show current quotes of all market makers in that security. The service will be provided through a desk top terminal connected to NASDAQ's computer complex. Level 3 is operated through essentially the same type terminal, but the user may enter his quote into the system.

So far, NASD and the Bunker-Ramo Corporation (which is designing and will operate NASDAQ) have concentrated on obtaining subscribers for the service in the New York City area. Efforts to obtain subscribers in other major cities are now underway.

FEDERAL RESERVE BOARD SETS OVER-THE-COUNTER MARGIN REQUIREMENTS

The Federal Reserve Board has set the final requirements for over-the-counter stocks to qualify under its new margin rules. The new regulations, along with a list of the stocks qualifying, were published on July 8. Only a few hundred of the thousands of nationally traded OTC stocks have been affected initially.

Listed below are the final criteria adopted by the FRB for OTC stocks to be eligible under its new margin provision.

1. The stock must be registered with the SEC and the company must have one million dollars of capital and surplus.
2. There must be five or more market makers.
3. There must be 1,500 or more stockholders who are not officers, directors, or beneficial owners of 10 percent or more of the stock.
4. The company, or a predecessor, must have been in existence for at least three years.
5. The stock must have been publicly traded for at least six months.
6. Bid and asked quotations are continuously available to the public.

The stock must also meet three of the following criteria:

1. There must be 500,000 or more shares of stock outstanding in addition to shares held beneficially by officers, directors, or beneficial owners of more than 10 percent of the stock.
2. The 500,000 shares described above must have an aggregate market value of at least ten million dollars.
3. The minimum average bid price in the last month, as determined by the FRB, is at least \$10.
4. The issuer had at least five million of capital surplus and undivided profits.

The new rules would exempt from margin requirements bank loans to broker/dealers against inventory positions when the credit is used to make a "bona fide" market in these securities.

In the unlikely event that a stock qualifies under the above rules but is not on the published list, an interested party can contact the Secretary of the Board of Governors, Federal Reserve System, 20th and Constitution Avenue, Washington, D.C. 20551, to petition that the particular stock be considered.

**BY-LAWS CHANGES
APPROVED BY
NASD MEMBERS**

All of the changes in the By-Laws and Rules of Fair Practice that were proposed at the May 28th meeting of the Board of Governors have been approved by the membership and the Securities and Exchange Commission with the exception of a proposed language change in Article V of the Rules of Fair Practice which was rejected by the SEC. The changes will be effective as of September 1st.

The three most significant changes in the By-Laws are:

- a. The Board of Governors will be increased from 23 to 24 members. The new governor will be a governor-at-large and will be selected from an insurance company or insurance company members. This change has resulted because of the dramatic increase in insurance company involvement with equity products and the corresponding increase in insurance companies as NASD members. The new governor will give these members the opportunity to participate more actively in determining Association policy.
- b. The Secretary of the Association will be required to notify Chairmen of the District Committees by June 1 when a Board member's or a District Committee member's term will expire during the coming year. The District Committee Chairmen will then have the responsibility to appoint a nominating committee which will have until September 1 of each year to report its selection. This will give members three months to submit candidates and also give the committee time to thoroughly review all names submitted.
- c. Because of the large number of "fails," the time that an emergency rule will be in effect without further Board action will be extended from the present 60 days to six months. The Board will be required to review the circumstances causing the emergency at least every six months and could terminate the rule at any time if it found the emergency no longer existed.

An important change that will affect the By-Laws and the Rules of Fair Practice jointly is: The maximum fine for each violation will be raised from \$1,000 to \$5,000. There have been cases in the past where only one or a few violations were found which were serious enough to require a greater penalty than a \$1,000 fine per violation, but not severe enough to require suspension. It is expected that this amendment will give the Board a reasonable alternative in such cases.

One change will affect the Rules of Fair Practice alone. This amendment will permit gifts in the amount of \$25 or less to be accepted or given by a member or person associated with a member provided the gratuities are recorded. The amendment will also allow a person to receive salary payments from two members if he is employed by both. Such an agreement, however, must be spelled out in detail.

**VARIABLE CONTRACTS
COMMITTEE NOMINATES
NEW GOVERNOR-AT-LARGE**

The Variable Contracts Committee met recently in Phoenix, Arizona to submit a list of nominations for a new Governor-at-large to represent the insurance industry on the Association's Board of Governors.

The membership has approved a By-Law Change proposed by the Board at their May meeting enlarging its representation to include this new and important segment of the securities industry.

Selection of the new Governor will be announced at the Board of Governors' meeting, September 22-24 at Colorado Springs. The Board will also announce at that time the new Chairman and Vice Chairmen to serve during 1970. Seven new Governors will also be elected and the results will be announced at that time.

**COURT RULES BANKS
AND SAVINGS & LOANS
CAN SELL MUTUAL FUNDS**

On July 1, the United States Court of Appeals for the District of Columbia ruled that banks may legally engage in operating mutual funds.

This decision resolved three separate cases: the Investment Company Institute vs. the Comptroller of the Currency; the Investment Company Institute vs. the First National City Bank of New York; and the NASD vs. the Securities and Exchange Commission.

These cases contested the legality of a bank's selling co-mingled investment funds (specifically the First National City Bank) under the Glass-Steagall Act and the Investment Company Act.

The court stated that it realized that these funds were a departure from traditional banking practices. However, the court was persuaded that regulation by the Comptroller of the Currency and regulation under the Securities Act would assure proper management of the funds.

The court saw no reason to disagree with the decisions of the Comptroller and the SEC that co-mingled investment accounts were both authorized by law and in the public interest.

The final outcome of all three cases is uncertain at this time. It is possible that the Mutual Fund Bill, passed by the Senate and now pending in the House, may be approved, thus permitting banks to operate co-mingled funds. In addition, the Bill would allow savings and loan associations the same privilege. Passage of the Bill, of course, would make an appeal to the Supreme Court pointless.

The NASD is expected to shortly announce whether it will seek review by the Supreme Court.

**ATTENTION
NASD
MEMBERS:**

Please send all due bill checks owned Direct Clearing Members on Stock Clearing Corporation balances to Direct Clearing Department, 44 Broad Street, 4th Floor, New York, New York 10004, Attention: Dividend Department.

New Form Will Require Report on Income And Expenses

In summer of 1968, the Securities and Exchange Commission adopted Rule 17a-10 which requires broker/dealers to report on income expenses. In connection with this rule, the NASD Form 17A-10 must be filed within 90 days of the close of the calendar year, in this case on or before March 31, 1970. The new form does not replace Form X-17A-5 which must still be filed (with SEC) once each calendar year.

The period to be covered by the new form is a calendar year, the first being 1969. Reports based upon fiscal years will not be acceptable.

Members can file with the NASD office in Washington, D.C., or with a national securities exchange if the firm is a member of an exchange having an SEC approved plan under Rule 17a-10. In the latter case, report forms will be supplied by the exchange. Edited copies of the report will be given to the NASD by the exchanges.

The following breakdown indicates the parts of the form that must be used by firms when filing with the NASD:

IF . . .	THEN FIRM MUST FILE . . .
A. (1) No securities transactions were effected with or for any person other than a broker or dealer (but see E. below), <i>OR</i> , (2) Gross securities income was under \$20,000.	Only Introductory pages
B. (1) Gross securities income is at least \$20,000, but under \$100,000, <i>OR</i> , (2) Firm has gross securities income of at least \$20,000 and received 80% or more of such income from <i>one or more</i> of the following: —retail mutual fund sales; —municipal bonds; —fractional interests in oil, gas, or other mineral rights; —variable annuities; —savings and loan placements; —real estate syndications.	Introductory pages AND PART I
C. (1) Firm does not qualify to file Part I, AND (2) Gross securities income was at least \$100,000, but under under \$1 million.	Introductory pages AND PART II
D. Firm does not qualify to file Parts I or II, or introductory pages alone.	Introductory pages AND PART III
E. Firm is an exchange specialist, floor trader or underwriter of shares of open-end investment companies or variable annuities who does not effect retail sales of such securities.	Introductory pages AND Special form being prepared by SEC

Any questions should be addressed in writing to Ralph E. Burgess, Chief Economist, National Association of Securities Dealers, Inc., 88 17th Street, N. W., Washington, D.C. 20006.

The NASD is awaiting the final form prepared by the SEC in order to coordinate the NASD companion form 17A-10 with the SEC requirements. The SEC has informed the Association that this material will be available soon.

Copies of NASD Form 17A-10 will be sent to all members immediately on completion.