

NASD

News

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NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. 1775 17TH ST. N.W. WASHINGTON, D.C.

To NASD Members and Registered Representatives:

NASD MEMBERS URGED TO ORDER CUSIP DIRECTORIES

The attack on the paperwork problem in the securities business is being waged on many different fronts. Although brokerage firms have had a respite because of the slackening in volume, preparations for efficiently coping with possible increase in volume must be considered top priority.

One of the programs which the Association is urging its members to support *now* is the CUSIP program, which will eventually encompass a universal numbering system for securities, broker/dealers and banks, and stockholders.

Management of the project is in the hands of the CUSIP Agency. The Agency's 15-man Board of Trustees consists of representatives from the banking industry, the Association of Stock Exchange Firms; the American, New York, Pacific Coast and the Midwest Stock Exchanges; the Investment Bankers Association and the NASD. Lee Monett, an NASD vice-president based in New York, is serving as the Association's representative.

The actual work of assigning numbers and descriptions is being handled by Standard and Poor's CUSIP Service Bureau. The CUSIP Directory, published last summer, contains numbers and alphabetic descriptions for more than 45,000 issues of stocks and bonds of 22,000 corporate issuers and 40,000 municipal issuers.

There are two versions of the Directory—the Corporate Directory and the Master Directory—both available in print or magnetic tape form. The Master Directory, which includes numerical designations for corporate and municipal securities is available for \$560 per year. A subscription to the Corporate edition, which excludes municipal securities, is \$400 per year. A subscription includes an updating service to keep subscribers abreast of new issues and their CUSIP numbers in advance of their sale.

Work is now in process to provide the same type of universal numbering system for broker/dealers and banks, and the directory containing this information is expected to be published this year.

NASD members will find it to their advantage to subscribe to this service now, since in any automated securities handling system, machines will be geared to processing numbers, *not* names. It is anticipated that the CUSIP identification system will eventually be utilized by all banks and brokerage firms in the country, so familiarization with its procedures is particularly important.

For further information or to order the Master or Corporate Directories, contact James M. Garnett, Director of Marketing, CUSIP Service Bureau, Standard Statistics Company, Incorporated, 345 Hudson Street, New York, New York, 10014.

**INTER-INDUSTRY GROUP
IS ORGANIZED TO DEFINE,
SOLVE MUTUAL PROBLEMS**

A joint industry committee composed of top-level executives from the securities and banking industries was recently organized to define mutual problems involved in handling securities transactions and to arrive at common solutions.

Called BASIC (Banking and Securities Industry Committee), the organization will be sponsored by the NASD, the New York Clearing House Association, the New York Stock Exchange, and the American Stock Exchange.

The major objectives of the organization will be to develop inter-industry concepts so securities transactions can be settled through improved procedures; to possibly develop a stock certificate that can be read by man and machine; and to plan for systems to process securities transactions of the future. The committee will utilize work being done in these areas by other industry groups. The Chairman of BASIC, John M. Meyer, Jr., is also chairman of the New York Clearing House Committee and Chairman of the Board of Morgan Guaranty Trust Company in New York.

Other members of the committee are: Richard B. Walbert, President of the NASD; Robert W. Haack, President of the NYSE; Ralph S. Saul, President of the American Stock Exchange; William H. Moore, Chairman of the Board of Bankers Trust Company; Walter Wriston, Chairman and Chief Executive of the First National Corporation; and Herman W. Bevis, retired Senior Partner of Price Waterhouse & Co. Mr. Bevis will serve as a full-time executive director for the group.

**CORPORATE FINANCING
GUIDELINES OFFER
PRACTICAL STANDARDS
FOR UNDERWRITERS**

Earlier this month, the Association's new Corporate Financing Guidelines were mailed to members. The Guidelines, which are based on the practical experience of the Committee on Corporate Financing's review of underwriting arrangements, have been designed to give members a practical yardstick to measure what the Committee considers to be within the Association's ethical standards.

Those firms involved in the underwriting of new issues and any firm that participates in any way in a public offering should become totally conversant with the guidelines. Among the important provisions are sections which (1) Increase the responsibility for fair underwriting arrangements to all members involved in any way in the preparation or distribution of a securities issue; (2) Limit the amount of securities that can be acquired by these persons in connection with a particular offering to 10 percent; and (3) Discourage a member from underwriting its own securities, directly or indirectly, or from participating in the distribution of these securities. Details of these and other provisions are spelled out in the guidelines.

Accompanying the guidelines was a new statement of policy issued by the Board of Governors which imposes certain limitations on venture capital and other investments by broker/dealers before a public offering. This statement specifies an adequate holding period for these investments before they can be sold and also discourages members from acting as underwriters or participants in the distribution of an issue in which they are selling stockholders.

Both documents will soon be incorporated into an NASD Manual Supplement.

LETTERS TO THE EDITOR

A number of letters to the editor have been received regarding the suspension of a principal for selling mutual funds below the breakpoint which was publicized in the January issue of the NEWS. Rather than printing each letter and a corresponding reply, we feel that a comprehensive answer to the many questions raised by this case would be more pertinent. Contrary to the opinions expressed in some of the letters, the Association would like to stress that any letter signed by a customer does not necessarily absolve a registered representative from his ethical responsibility toward his customers.

The case in point fell under the Association guidelines which stress that the sale of investment company shares in dollar amounts just below the point at which the sales charge is reduced on quantity transactions is contrary to just and equitable principles of trade.

In this case, it was determined at the District Committee level that the principal had a documented history of selling investment company shares in dollar amounts below the breakpoint in order to receive higher sales commissions. From an NASD examination of his firm's records, it was discovered that in at least eight separate accounts, the principal had directed his customers' purchases to more than one investment company and to mutual funds which represented the same type of investment objective.

Through the Association's computations, it was determined that the customers in these accounts might have collectively saved \$11,000 if their investments had been consolidated into one investment fund or one management company. In all but two examples, there was no evidence that the principal had divulged information prior to the customers' investments concerning how they could have taken advantage of the existing breakpoints and the accompanying lower sales charges.

The principal of the firm involved argued that his customers were sophisticated investors and that he had explained and they understood the significance

of the breakpoints, but decided to ignore the possible savings in order to invest in various mutual funds according to their own desires. It was his contention that it was his duty to implement their wishes, even when it was not to their advantage. He then produced notarized statements from some of these customers stating that they knew about and were willing to pay the higher charges. *These statements were obtained after the transactions had taken place.*

After examining the accounts and the notarized documents, the DBCC and the Board of Governors determined that the investors were not sophisticated investors and that the principal had not adequately explained the principle of breakpoints to them. It was also determined that, in some of the accounts, the principal was a controlling force in deciding the investment vehicles. After considering the facts, the DBCC and the Board determined that the principal was guilty of a breach of the NASD Rules of Fair Practice.

Statements in some of the letters that we received in response to this case espoused the philosophy of "caveat emptor"—let the buyer beware. On the contrary, the Association stresses that it is a broker/dealer's responsibility to make the buyer *aware*. Each broker/dealer is morally, legally, and ethically bound to serve the best interests of his customers and in this regard to protect the customer from his own ignorance.

In one of the letters, we were asked if a firm should refuse an order if a customer asked to purchase several mutual funds although he was told that he would pay lower charges by purchasing one fund.

Our answer is, "not necessarily." Diversification can be desirable. An investor may have more than one investment purpose, and it may be best for him to invest in various funds to meet his various objectives. Occasionally, it may even be desirable for an investor with one specific investment objective to invest in several different funds to obtain diversification of management.

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There are no guidelines that can be applied across the board for all investors. Each investor's goals must be weighed against the facts in a given case. Most importantly, a broker must give objective advice to help an individual obtain his goals.

The best protection for any broker is to know his customer—to judge his level of sophistication in the investment area, and to serve him accordingly.

However, there is one suggestion that the Association can make in regard to an investment that a client insists on making although his broker has advised him that it would be unsuitable. First, we recommend that a broker use all his persuasive powers to channel an investor into investments compatible with his goals.

If the customer refuses to accept the broker's ad-

vice, we suggest that the broker compose a statement containing his reasons for objecting to the investment and mentioning that his firm will not be responsible for the possible consequences of the customer's actions. He should then have the investor carefully read the statement and sign it in the presence of a notary public. This should be done prior to the transaction. The broker, of course, has the alternative of refusing the customer's business.

This is merely a suggestion—not a guideline. Again, a broker must make a judgment depending on the individual customer.

We would also like to stress that, if a broker has a specific question concerning Association policy, that he can contact the NASD District Office in his area or the Department of Regulation in the Executive Office in Washington, D.C. to ask for assistance.

MANAGEMENT & SUPERVISION

NOTES

NASD FINANCIAL REPORTING FORMS MAILED TO MEMBERS

NASD members will soon be receiving a package in the mail which will include a cover letter, the new financial reporting form (NASD Form 17A-10) which members will file with the Association, and a detailed explanation telling how the forms should be completed. The form is an outgrowth of the Securities and Exchange Commission's rule 17a-10 requiring complete financial information from all brokerage firms. The resultant data will be used by the NASD for various industry studies and management guides. All NASD members will be required to fill out designated sections of the form with the exception of those members that also belong to another self-regulatory agency and file a similar report, approved by the SEC, with that agency.

Data from the NASD forms must be transmitted to the SEC, however, none of the firms will be identified. The initial financial information requested will pertain to operations during 1969, and the deadline date for return of the form is April 30, 1970.

The form, which is divided into an introduction and three parts, may appear to be a formidable project for member firms. However, many members will need to file only the five-page introduction, and other members will file the introduction plus one of the other three sections.

CHANGES ANNOUNCED IN UNIFORM PRACTICE CODE

Certain changes to the Uniform Practice Code have recently become effective.

Section 4 (e), "When as and if issued" now includes the provision that delivery of new issues to members who are not part of the syndicate or selling group shall be made during normal delivery hours.

Section 29 (g) has been extended to emphasize that it is not necessary to have guarantees from "New York" banks or exchange members in order for a certificate to be in good deliverable form.

Section 48 (f) has been added in order to make explicit the availability of the buy-in procedure where a member has defaulted on a due-bill situation for rights, stock or script.