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### Qualification Examinations

**Boston, Philadelphia Centers Established; New York Area Expanded**

Qualification examination centers under direct NASD supervision have been established in Boston and Philadelphia, thus expanding to New England, Eastern Pennsylvania and Delaware the areas in which persons seeking to enter the securities business will be tested under controlled conditions.

Until now, the only examination centers have been in New York City, at Hunter College and New York University. Elsewhere, applicants seeking to become registered representatives of members have been taking the qualification examinations in the offices of their intended employers.

Other examination centers shortly are to be established in upper New York State, Atlanta, and on the Pacific Coast. The ultimate objective is to have examinations given under controlled conditions at convenient locations throughout the country.

Under the new arrangement, applicants from the Eastern part of District 12 will normally take their examinations at the Philadelphia center. However, if they happen to be in New York on the day appointed for the examination, they may take the test at one of the two Manhattan centers.

Similarly, if an applicant from Vermont is in New York on a day scheduled for the examination, he also may be examined at one of the centers there, rather than make a special trip to Boston. By the same token, an applicant from Connecticut may prefer to take the examination at the District 14 office in Boston rather than in New York City. This flexibility will be extended as more examination centers are established over the country.

The area covered by the New York City centers has also been ex-

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### Safety! Income! Capital Gains!

"Now you can have all three in one purchase. A first-rate sinking fund bond yielding 8% per annum. Plus common stock with a big capital gain potential, sold as a unit. The bonds represent safety. The dividend represents income. The common stock represents capital gains. The income is secured, the speculation is free. Get the facts—judge for yourself! Send for free offering circular."

This eye-catching ad also caught the eye of a District Business Conduct Committee which, upon further investigation, found that it contained exaggerated claims and misleading statements, while omitting material facts. There was little safety for the member who prepared the ad—he was expelled!

### "Continuing Commissions"

The Board of Governors, in response to many inquiries, has held that the payment of continuing commissions in connection with the sale of investment company shares is a proper practice only so long as the person receiving the commissions remains a registered representative of a member of the Association.

Effect of this Board opinion is that members of the Association may not vest in any person, by agreement, contract, or otherwise, rights to continuing commissions on either voluntary or contractual plans for the purchase of investment company shares unless the person to whom the commissions are to be paid is a registered representative of a member at the time of payment.

In other words, registration *must* be maintained by any person who is to receive commissions.

### Redistricting Progress

**Members to Vote on New Alignment of Association**

The Board of Governors has unanimously adopted a plan to reshape the geographical outlines of the Association's Districts.

Under the proposal, a number of the present Districts will be reconstituted with different boundaries, resulting in thirteen Districts instead of the present fourteen.

Major purposes are to modernize the organization of the Association at the local level for more efficient handling of administrative work by District Committees and to adjust the District representation on the Board of Governors to reflect the present distribution of Association membership throughout the country.

District boundaries were originally set in 1939, when there were 2,600 members of the Association. Now there are 3,800 members, and this 50 percent increase has resulted in some disparities that need to be corrected.

A new section and several revisions of Article IV of the By-Laws are required to implement the plan approved by the Board. The new section describes in detail the proposed procedures for the election of District Committeemen and Governors to take office in January 1959, for the Districts that are affected by the redistricting. Other proposed changes are technical, but are essential to make the By-Laws consistent with the plan approved by the Board.

These proposed changes in the By-Laws are being submitted to the membership for vote, together with a complete explanation of the Redistricting Plan.

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panded to include Delaware, Schoharie, Schenectady and Rensselaer Counties and the area south of these counties in New York State. Applicants from cities in this area, such as Albany, Schenectady and Troy, will no longer take the examination in the offices of the firms that plan to employ them.

The rate of failures is four times as high at examination centers as when the tests are given in members' offices. The Board of Governors' action last year in raising the passing grade for qualification examinations from 65 to 70, and the use of more difficult examinations, also contributed to the substantial rise in failures.

In the first five months of this year, 136 failures were recorded, against 81 in all of 1957. The annual rate of examinations scored remains about the same at approximately 14,000.

## Important Keystone

Willful failure of NASD members to file annual financial reports is ground for expulsion from the Association, according to a recent SEC opinion.

The action gave formal recognition to the importance of the Commission rule requiring broker/dealers to file annual financial reports. Said the SEC:

"The requirement that annual financial reports be filed is an important keystone of the surveillance of registrants and NASD members with which we and the NASD are charged in the interest of affording protection to investors, and it is obvious that full compliance with this requirement must be enforced."

The Commission found that a broker/dealer had wilfully failed to file the required statements and that it was in the public interest that his registration be terminated. He was given opportunity to withdraw his registration and did so. Had he not, the SEC was prepared to revoke his registration and expell him from NASD membership.

## More Issues Wanted

### Quotations Groups Give Listing Needs

The Regional Committees supervising the NASD's Eastern, Midwestern, Pacific Coast and Southwestern quotations are looking for additional securities that may be added to the lists of quoted issues.

Members who know of an issue that may meet the requirements and would like the security to be quoted in *The Wall Street Journal* and other publications should apply to their Regional Quotations Committee through the appropriate District Office. Applications that qualify for the National List will be referred directly to the National Quotations Committee by the Regional Quotations Committees.

The requirements for the Regional Quotations Lists are, in general, as follows:

- Minimum of 300 stockholders in the region for the Pacific Coast and Midwest; 200 and 500 stockholders, respectively, for the Southwestern and Eastern Lists;

- Minimum market value of \$500,000 for stocks and \$2,000,000 for bonds for the Eastern, Pacific Coast and Southwestern Lists; minimum of 50% stock outstanding or 100,000 shares for the Midwest;

- Dividend declaration policy must include publication of declaration at least a week prior to "record date" for Eastern, Pacific Coast, and Southwestern Lists; 10-day notice for the Midwest.

In addition, a minimum bid price of \$3 per share is required, and financial statements must be made available to the public at least once a year.

### "What You Must Know . . ."

For the first time, the Association has put together in one package most of the fundamental standards governing the offering of shares of investment companies. The publication, in booklet form, is designed as an additional service to members and their registered representatives.

The booklet contains text of the Securities and Exchange Commission's Statement of Policy, pertinent extracts from the NASD Manual, text of various SEC Rules and interpretations, and extracts from the statutes. In addition, a special sec-

tion has been incorporated giving specific examples of the right and wrong way to prepare sales letters, general and institutional advertising, radio material, and "tombstone" advertising.

Entitled "What You Must Know," the booklet was prepared under the auspices of the Investment Companies Committee, as authorized by the Board of Governors, on an 8½" x 11" format and in a large type size that should make for easier reading.

Copies have been sent to the members and branch offices, and additional copies are now available for distribution among registered representatives and key officers at 25¢ a copy.

The publication has received considerable favorable comment and it has been suggested that it should be particularly helpful to firms with substantial sales forces, since its contents apply not only to written material, but to oral presentations in behalf of investment company shares.

## Part-Time Dealers

The problems of part-time dealers who employ full-time salesmen but give them only part-time supervision will be studied by a special committee of the Board of Governors. Difficulties in this area of the business are now beginning to appear with some frequency.

The part-time dealers are generally new members who are already established in other fields, and have decided to add another string to their bows by carrying on a securities business as a sideline. Among such firms are travel agencies, insurance brokers and agents, and real estate operators. Even a surgeon is now a dealer on the side.

The special committee will study part-time problems in the industry as they apply both to members and to salesmen. In 1957, a special committee on part-time salesmen concluded that training and proper supervision were the important requirements, rather than full-time employment as a securities salesman. This decision was based, however, on the premise that full-time dealers who employ part-time salesmen would fully supervise those salesmen.

## Installment Contracts

### Warnings on Intrastate Securities Offerings

NASD members in District 3, Denver, have been warned to be especially careful in so-called "intrastate offerings" and in the sale of securities on installment contracts to avoid inadvertent violations of Federal law and Association Rules.

When securities are sold on an installment contract basis and there is inadequate disclosure in the offering circular either as to the amount of commission received by the underwriter in proportion to the initial sums received by the issuer, or as to penalty if the installment contract is not kept current, such offerings would be improper under the Rules of Fair Practice of the Association, a District 3 Committee memorandum said. This would be true whether or not the practice is permissible under the laws of the state.

The Committee also said every member should heed the following advice:

"A dealer participating in a distribution of an issue claimed to be exempt because offered only to residents of the company's own state or proposing to deal in such an issue within 40 days after its first public offering, should examine the character of the issue and its proposed and actual manner of offering with the greatest care to satisfy himself the distribution will not, or did not, involve the making of any sales to non-residents, or otherwise the dealer, even though his own sales may be carefully confined to resident purchasers, might subject himself to the risk of civil liability for selling without prior registration a security not in fact entitled to the exemption."

The Director of the SEC's Division of Trading and Exchanges, in a letter to the Executive Director of the Association, commended the Committee for taking the initiative in so warning its members. He also called attention to the recent Commission decision in The Whitehall Corporation case (Securities Exchange Act Release No. 5667).

In this action, the Commission held, among other things, that unless the assignment of a subscriber's

rights to obtain shares under an installment contract upon completion of the payments were effectively restricted to the residents of the state of the initial offering, the use of such installment arrangements made the intrastate exemption from SEC registration unavailable.

## NASD Office Moves

The Executive Office of the Association in Washington has moved.

New address of the headquarters of the National Association of Securities Dealers, Inc. is 1707 H Street, N. W., Washington 6, D. C.

The enlarged quarters were made necessary due to the substantial growth of the Association and the resulting inadequacy of the former office, which had been occupied for 10 years.

The telephone number remains the same—Executive 3-4970.

## Board Says "No"

Simultaneous transactions for the purchase and sale of securities at prices not related to the current market would violate the NASD Rules of Fair Practice, the Board of Governors held in a recent ruling.

A member proposed to buy from a life insurance company a block of ABC 2¾% bonds at 100 and simultaneously sell to the same insurance company a block of XYZ bonds at 100, when the market for both the ABC and XYZ bonds was 90. Thus, a premium would be paid for the ABC bonds purchased and a premium would be received for the XYZ bonds sold, enabling the insurance company to record the XYZ bonds at the same book value at which it was carrying the ABC bonds.

The member had informed the Association that the life insurance company would thus avoid a capital loss or charge to its securities valuation reserve and also show a lower yield on the bonds it purchased.

The Board unanimously found that the proposed transactions would violate Sections 1 and 4 of Article III of the Rules of Fair Practice, in that the prices of the bonds would not be reasonably related to the current market. Furthermore, the Board felt that to countenance such activity might, directly or indirectly, be permitting a violation of state insurance, banking or other laws.

## More on "Fails"

### Legal-Form Certificates May Force "Buy-Ins"

Due to the increase in fails to deliver and receive, especially those caused by certificates in legal form, the National Uniform Practice Committee urges members to make sure what form the certificates are in before introducing them into the market.

Members have been complaining to the Committee that many salesmen introduce stock into the market for "regular way" delivery, with the knowledge that it may take weeks or even months before the certificates will be in good delivery form.

The purchasing broker-dealer should be given the opportunity, at the time of transaction, to decide whether or not he wishes to make a trade involving stock that is in legal form, the Committee emphasized.

Members are always reluctant to "buy-in" but, if the practice continues, purchasing broker-dealers may be forced to employ the "buy-in" procedure of the National Uniform Practice Code.

## New Book

"Investment Banking Functions," by Merwin H. Waterman, Professor of Finance, University of Michigan, has just been published. Professor Waterman traces the functions of the investment banker from the early evolution of the business in this country to the present time.

The project was sponsored by the securities business through the Joint Committee on Education, and was financed by the NASD, other associations, stock exchanges, and individual firms. It is a publication of the Bureau of Business Research, School of Business Administration, University of Michigan, and is priced at \$4 in cloth, \$2 in paper cover.

## "Facts" Folder

The Association still has a limited supply of the folder, "Facts About the NASD," which briefly describes the Association, and tells what it does and how it does it. This informative folder was designed for use with customers as well as with new employees. Free copies are available from the Executive Office as long as the supply lasts.

## Variable Annuities

### High Court Review to be Sought; 1959 Argument Seen

The NASD and the SEC will ask the United States Supreme Court to review the adverse decision of the Court of Appeals for the District of Columbia in the joint Association—government effort to have “variable annuity” contracts declared securities. Should the Supreme Court grant a review of the case, argument before the Court probably will not take place until the Spring of 1959.

The District Court originally held in this key case that “variable annuity” contracts had many of the characteristics of a security, but that the McCarran-Ferguson Act specifically exempted the “business of insurance” from Federal control. The Commission and the Association had urged the Court of Appeals to find that these contracts are in fact securities, subject to the same regulatory controls that govern the sale of other securities.

The three-man Court of Appeals did not agree, holding instead that the contracts had many qualities of the traditional business of insurance and, hence, were not subject to regulation as securities.

The opinion was based partly on the Court's finding that since the insurance commissioner in the District of Columbia had subjected the business of Variable Annuity Life Insurance Company of America to his supervision, the Court should not over-rule the insurance commissioner.

In another development, the State Securities Commission for West Virginia notified the NASD that trial in the suit brought for an injunction against the sale of VALIC contracts in that state was to commence July 21. The Association's counsel was invited to participate and the Association is cooperating fully with the State officials.

A similar case in Virginia was delayed at the request of VALIC until the Federal case has been finally decided.

There has been activity in various state legislatures involving the jurisdiction of state officials over “variable annuity” contracts, and the NASD is following these developments closely.

HARRY G. RITER, III



Harry Riter, 1943 Chairman of the NASD Board of Governors, died June 30 after a brief illness. President of the National Association of Manufacturers in 1955, Mr. Riter for years was senior partner of Riter & Co., prior to joining Thomas A. Edison, Inc.

## Radio, TV Scripts

Members who sponsor radio and television programs should be aware of the Board of Governors' interpretation with respect to advertising (Pages E-140 and E-141 of the Manual) when preparing their commercials and program material. The interpretation applies to radio and television broadcasts, as well as to sales literature and advertising regarding all securities except investment company shares.

A copy of the text of commercials and program material should be maintained in members' separate Advertising Files for twelve months from the date of use.

## Trial Balances

The SEC has amended its books and records rule to require brokers and dealers to prepare and maintain a record of the proof of money balances of all ledger accounts, in the form of trial balances, currently at least once a month. This amendment to Rule 240. 17A-3 does not require any additional filing with the Commission. It became effective July 1.

## Non-Member Business

### Board Position on Transactions with Firms Outside Association

Members of the Association may not obtain for their customers shares of investment companies from underwriters, distributors or sponsors which are not members of the Association, the Board of Governors has determined.

This policy action has the effect of prohibiting members from purchasing for customers—or making any arrangement for customers to receive, acquire or purchase—the shares of those investment companies whose underwriters are not members of the NASD.

In taking this position, the Board invoked Section 25(b)(2) of Article III of the Rules of Fair Practice. In essence, the Board said it is immaterial whether there is any service charge or fee in connection with such transactions.

Several District Business Conduct Committees, meanwhile, have found it necessary to call the attention of members to the basic rules of the Association relating to dealing with non-members. Section 25 of Article III, in general, sets forth restrictions on the granting of concessions, discounts or other allowances; on joining with non-members in distributions; and on trading with non-members at prices other than those granted to the general public.

The applicability of this Rule is well explained in a memorandum on Pages E-101—E-106 of the Association's Manual. Members are cautioned to give Rule 25 and the explanatory memorandum a careful reading.

## "Free-Riding"

Twenty-four complaints have been filed and 45 letters of caution written by District Business Conduct Committees in connection with member activities in the recent underwritings of the securities of Carter Products, Inc., Florida Steel Corporation, and American Heritage Life Insurance Co.

The District Committee actions cited violations of the Board's interpretation of the Rules of Fair Practice with respect to “free-riding.”