

OPENING STATEMENT

by

Mr. Avery Rockefeller, Jr., Chairman of the Board of Governors  
National Association of Securities Dealers, Inc.

at

Public Hearings conducted by the  
SEC's Special Study Group on Qualification and Training  
May 22, 1962

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I am Avery Rockefeller, Jr., of New York City, Chairman of the Board of Governors of the National Association of Securities Dealers, Inc. I am accompanied today by Wallace H. Fulton, Executive Director of the Association, Marc A. White, Counsel to the Association, John H. Hodges, Jr., Special Assistant to the Executive Director, and Ray Moulden, Secretary of the Investment Companies Committee.

Since the topics to be covered in this hearing include qualifications, training and testing of registered representatives, I believe it may be helpful to describe briefly the manner in which NASD activities in the field of testing have developed since 1940, the first year of Association operations.

Initially, only firms were registered with the NASD. It became apparent, however, as the Association gained experience in disciplinary matters, that control was needed directly over those who dealt with the public. For this reason, the Board sought from the SEC the right to require the registration of each partner, officer, salesman, trader and those in supervisory positions. Article XV of the By-Laws was approved by the membership and with the authorization of the SEC, individuals employed by members in the capacity of a registered representative were registered with the NASD for the first time in January, 1946.

Our policy in the field of accreditation was formulated in May, 1955, when the membership approved an amendment to Article I of the By-Laws which would require new persons entering the securities business as registered representatives to pass a written examination. The purpose of the test, as set forth in the By-Laws, was to have new applicants for registration demonstrate that they have the technical proficiency and knowledge of the securities business necessary to conduct a business or to perform their duties and functions.

The examination questions, however, were required to be incorporated by reference as a part of the Association's By-Laws. Consequently, in order to establish a qualification examination, it was essential to obtain the permission of the SEC and, furthermore, to have the SEC review each question in the examination. Permission to establish a qualification examination was granted with the provision that the questions and answers be included in a pool of questions and made available to the applicants.

Most applicants, of course, read only the pool of 440 questions and answers which were published in a booklet. As a result, the test failed to provide the incentive for intensive study of the securities business, which was the sole purpose of the examination.

Within the limitations which were placed on the old test program, the Board continually worked to strengthen it. On June 1, 1956, the date the first examination was introduced, the passing grade was 65 per cent. A year later it was increased to 70 per cent, and on October 1, 1959, it was set at 80 per cent.

Also, in the beginning, most examinations were taken in members' offices. Today all tests are taken under uniform controlled conditions at examination centers. We now have 65 centers located mainly in colleges and universities, and tests taken in foreign countries are monitored by the United States Consular Service.

In November, 1960, the SEC staff advised us that it would no longer be necessary to publish the questions and answers, and two months later, in January, 1961, the Board approved the employment of The Psychological Corporation to prepare a new examination. During 1961, some 7,000 individuals participated in the experimental testing of more than 600 trial questions. Results from the testing sessions were analyzed with the help of IBM computers to determine the degree of difficulty of each question. All questions were also reviewed to be sure they were free of ambiguity. In place of the questions and answers booklet, a study outline and a list of reference materials were prepared for use as a guide by applicants in preparing for the test. The Study Outline was first sent to members on November 1, 1961.

The present examination was introduced on January 2, 1962. It consists of 125 multiple-choice questions with a two-hour time limit. There are three forms of the test currently in use. Each form contains different questions but covers the same subject matter areas. During the month of January slightly over 10 per cent of the applicants failed the test, which was three times the rate of failure during 1961 under the old test. The rate of failures then dropped to an average of 7 per cent for the period of January through April.

A waiting period was also established as a penalty for those who failed the new test. An applicant who has failed the test in his first attempt must wait 30 days before he can take the test a second time. A 60-day waiting period is required for those who fail in their second time, and a 90-day waiting period is required for those who fail in their third attempt.

The Board of Governors, in reviewing the performance of the new test at its meeting on Wednesday, May 9, concluded that the initiation period should be considered over and voted to increase the passing score, which will result in a higher failure rate. This increase will be made effective as soon as it can be cleared with the SEC. The actual passing score as well as the questions and answers are now accorded confidential treatment by the SEC, and test results are reported to members by letter grades A, B, C and F.

The Psychological Corporation is currently preparing new questions, and these are being trial tested at 14 of the NASD examination centers. We will, therefore, be able to prepare new test forms as soon as they are needed.

The objective of the Board of Governors is to continually increase the standards of knowledge of those entering the business, and to this end, periodic increases in the passing score and the inclusion of more difficult questions in the examinations can be expected.

Several other matters in this field were also approved by the Board of Governors at its recent meeting.

The Board has authorized and directed that a new examination, preferably containing essay-type questions, be prepared for new persons seeking to enter the business as officers, partners or sole proprietors. This examination will cover in depth the responsibilities of principals in securities firms.

Also authorized at this meeting was the development of a detailed study plan which will be adaptable both as a home study course and as the basis for a classroom-conducted course. The study plan will set forth specific reading assignments, explain the relevance of material covered and include questions that may be used in checking for mastery of assigned subject matter.

The Psychological Corporation will be retained to work with us in the development of the essay test and the study plan.

In summary, we have made marked progress in the field of testing during the current year and are preparing to take additional steps to strengthen the program in the immediate future.

Thank you.