



Testimony

Of

Elisse B. Walter

**Senior Executive Vice President
Regulatory Policy and Programs**

**Before the
Committee on Financial Services
Subcommittee on Oversight and Investigations**

**Hearing on the Financial Services Needs of
Military Personnel and Their Families**

United States House of Representatives

May 18, 2006

Mr. Chairman and Members of the Subcommittee: NASD is grateful to the committee for inviting us to testify on NASD's regulatory activities regarding inappropriate sales of certain investment products to members of the armed forces and NASD's financial education programs focused on military servicemembers and their families, and for allowing us to submit this statement for the record.

NASD

Founded in 1936, NASD is the world's pre-eminent private-sector securities regulator. In 1939, the SEC approved NASD's registration as a national securities association under authority granted by the 1938 Maloney Act Amendments to the Securities Exchange Act of 1934. We regulate every broker-dealer in the United States that conducts a securities business with the public—about 5,200 securities firms that operate more than 108,000 branch offices and employ about 664,000 registered representatives.

Our rules regulate every aspect of the brokerage business. Our market integrity and investor protection responsibilities include compliance examinations, rule writing, enforcement, professional training, licensing and registration, dispute resolution and investor education. NASD examines broker-dealers for compliance with NASD rules, MSRB rules and the federal securities laws, and we discipline those who fail to comply. Last year, NASD filed a record number of new enforcement actions (1,410) and barred or suspended more individuals (830) from the securities industry than in any previous year. NASD has a nationwide staff of more than 2,400 and is overseen by a Board of Governors, more than half of whom are not in the securities industry. During the last four years, NASD has been in the process of separating from The NASDAQ Stock Market.

Executive Summary

America's men and women in uniform make great personal sacrifices to protect our nation's security. They should not have to worry about the honesty and integrity of those who offer to help them make sound financial decisions for themselves and their families. Yet thousands of mostly young servicepersons have been disadvantaged by inappropriate sales of products and services, including the sale of an investment product called Periodic Payment Plans or PPPs.

NASD learned in 2003 that a broker-dealer was targeting U.S. servicemen and women with these investment products, and was doing so using improper sales practices. We have responded forcefully to end these practices, sanction those responsible for them, ensure that their victims are recompensed for their losses, and educate military personnel broadly about saving and investing.

My testimony today will focus on this last item—our recently launched efforts to educate servicepersons and civilians so that they are able to avoid fraudulent and inappropriate products and sales pitches.

By way of background, First Command Financial Planning Inc. of Fort Worth, Texas, a broker-dealer with many ties to the military, using misleading sales pitches and improper sales tactics, had targeted and sold more than a half-million of complicated and often extremely expensive PPPs to servicepersons, many of whom were young and inexperienced investors. An investor in a PPP makes monthly payments of as little as \$50 for a fixed time period, usually 15 years. The payments are invested in mutual funds and the investor is charged a 50 percent sales load or up-front fee on the first year's payments. Payments during the remainder of the 15-year term are not subject to sales loads, so that the effective sales charge decreases if the investor continues to make contributions. However, if the investor stays in the plan for more than 45 days, yet fails to make contributions over the full 15-year term, he or she can pay a sales charge of up to 50 percent of the total amount invested.

After a thorough investigation, including taking testimony from 16 current and former First Command employees, reviewing more than 25,000 pages of documents and over 50,000 email messages, NASD brought disciplinary action against the firm. NASD coordinated its activities with the SEC and both cases against the firm were announced on the same day.

The firm was censured and fined \$12 million in December 2004. That amount included restitution to thousands of customers who had terminated PPPs after January 1, 1999, and had paid effective sales charges greater than five percent. By February 2006, more than \$4.4 million had been returned to these customers. About \$6.8 million was transferred to the NASD Investor Education Foundation to be dedicated to financial education programs for members of the armed services and their families.

First Command has informed NASD that it has ceased selling PPPs. That firm, however, was not the only firm selling PPPs to military servicepersons. NASD has ongoing investigations of additional firms that also sold the plans, although most of them have now stopped. Statistics show that the rate of new PPP account openings at one of the largest sponsors has dropped from about 1,000 per month to about 10 per month.

The First Command case vividly illustrates the need for the education and protection of military servicepersons and family members who invest in securities. Since our settlement with First Command, NASD has devoted a great deal of time, money and attention to developing a far-reaching program for providing financial education to military servicepersons and their families.

NASD Investor Education Foundation

NASD established the NASD Investor Education Foundation in December 2003, inspired in part by survey data, which showed that mainstream investors had a troubling lack of knowledge and understanding of markets and investment products. Since then, we have contributed \$31 million to the NASD Foundation. Last year, the SEC filed a motion with the federal court handling the Global Research Analyst Settlement, requesting the transfer to the NASD Foundation of the approximately \$55 million in investor education

funds in that settlement. In September 2005, the court approved the SEC's request, and the funds should be transferred in the near future.

Through its grant making, the NASD Foundation funds programs that provide information and resources to audiences typically underserved by financial education programs. More than \$4.5 million dollars has been awarded to organizations for educational programs and research projects that reach out to, among others, minorities, young investors, Native American communities and the elderly.

Research grants offer experts a chance to provide insight into how investors make decisions, what information they need to make better-informed decisions and how to create better learning environments. Recent grants include:

- University of Connecticut is conducting experiments that manipulate the visual display of Web-based disclosure information to determine investor preferences, and the effect on comprehension and retention of disclosure information.
- Princeton University is examining psychological biases that play a role in poor investment decisions and developing and testing a set of interventions to promote wise investing by mitigating these biases.

Grants awarded to educational projects aim to create and expand investment resources for populations most in need. Recent educational grants include:

- Collaborating with the University of Florida, Kansas State University and the University of Kentucky, the University of Tennessee will develop a workplace investor education program for young adult workers in Florida, Kansas, Tennessee and Kentucky.
- WISE Senior Services of Santa Monica, in collaboration with the AARP Foundation, is examining the susceptibility of the elderly to fraudulent investment solicitations.
- As part of its successful *Building Native Communities* financial education series, First Nations is producing an educational curriculum called *Investment Skills for Families* and training an initial pool of Native Americans to deliver the new material.

SaveAndInvest.org

As mentioned above, approximately \$6.8 million of the First Command settlement funds has been transferred to the NASD Foundation and specifically earmarked for programs designed to help members of the military and their families better understand basic financial concepts, including saving, investing and the markets.

Many servicemembers report having difficulty covering expenses and saving for the future. Research conducted in June 2005 found that only 29 percent of military personnel who currently invest received a passing grade on a quiz about basic financial knowledge. However, 58 percent of survey respondents said that it was very important to them that they become more knowledgeable about saving and investing. Sixty-two percent indicated that they plan to increase their investment levels in the next year.

Working closely with the Department of Defense, the NASD Foundation launched a multifaceted military financial education program early this year. This comprehensive campaign to help servicemembers and their families manage their money with confidence is being implemented on military installations worldwide. It encourages members of the armed forces to take control of their financial futures—by providing them and their spouses with financial information to help them make intelligent saving and investing decisions.

The multifaceted program includes:

- an online resource center, www.SaveAndInvest.org, that serves as a centralized, trusted source for unbiased information on saving and investing, including original content, interactive tools/games, partner resources, frequently asked questions, and more;
- on-the-ground training to support the military's current Personal Financial Management program by establishing a coordinated and uniform financial education program, including the training and continuous certification of personal financial counselors and other volunteers;
- a spousal fellowship program that will train a corps of military spouses to provide financial counseling and education within the military community;
- a print and online publication that helps servicemembers and their families deal with the financial issues surrounding deployment and duty-station changes; and
- partnerships with the Department of Defense, the U.S. Securities and Exchange Commission, the National Military Family Association and other organizations whose expertise in the financial education arena and experience in addressing military audiences complement the NASD Foundation's commitment to providing financial education information and resources to servicemembers and their families.

To ensure that these programs and tools are well exploited by the military community, the NASD Foundation's efforts include a long-term, public awareness campaign that will:

- provide a coordinated, national financial literacy campaign to a military population that is often unable to set and achieve financial goals, unwilling or

unable to save, overextended in debt, vulnerable to fraud and unaware of what can be done to gain control of the situation;

- help military families understand how the financial choices they make can either improve or diminish their ability to achieve goals such as homeownership, a college education, a secure retirement and peace of mind; and
- communicate positive and motivational messages in a variety of ways and through a diversity of media so that everyone in the military has the opportunity to see, understand and act upon them.

Soon after launching SaveAndInvest.org in January 2006, an NASD Investor Education Foundation team traveled around the world to conduct a series of free financial education forums at bases and duty stations in the United States and far beyond our borders. The first of these free forums, a multi-service event, took place in Honolulu, Hawaii; followed quickly by programs at Camp Foster (a U.S. Marine Base), Okinawa, Japan; Yokosuka Naval Base, Yokosuka, Japan; and aboard the San Diego-based USS RONALD REAGAN, now on a tour of duty in the Arabian Gulf.

The Honolulu financial education forum was offered in partnership with Military Family Support Centers serving the Air Force (Hickam Air Force Base), Army (Schofield Barracks), Coast Guard (US Coast Guard-District 14), Marine Corps (MCB Hawaii) and Navy (Pearl Harbor). It was attended by almost 500 members of the military and their families. The event drew attendance from all branches of the U.S. military and Coast Guard. The others programs have drawn almost 1,300 additional members of the military and their families.

At the forums, presenters from NASD covered topics including fundamental principles of saving and investing, how to check the background of your broker or firm, and how to use NASD's mutual fund expense analyzer, a Web-based tool developed by NASD. In addition to this general information, NASD and representatives of the Securities and Exchange Commission and the Hawaii state securities regulators presented financial seminars including:

- Smart Saving and Investing—Avoid the Predatory Loan Trap;
- What to Look for in an Investment Advisor;
- Mutual Funds, 529 Plans and More;
- Bond Investing: the Basics and Beyond;
- Annuities: What You Should Know;
- Stock Trading and the Anatomy of a Stock Scam; and
- Smart Saving for Retirement.

The sessions were well attended and gave attendees an opportunity to receive detailed information and ask specific questions pertaining to their own financial situations.

Aboard the USS RONALD REAGAN, the goal of the three-person NASD team was to integrate itself into the life of the aircraft carrier. Presentations were made virtually around the clock in an effort to reach both day and nightshift personnel. In all,

close to 30 presentations were made during the three days aboard ship, attended by approximately 1000 members of the REAGAN crew. In addition to the core presentations on Predatory Lending, Smart Saving for Retirement and Smart Mutual Fund and 529 Investing, the team provided seminars on Smart Bond Investing, Annuities, Nuts and Bolts of Mutual Fund Share Classes and Expenses, How to Select a Broker or Financial Professional, and Stock Trading and the Anatomy of a Stock Scam.

The NASD Investor Education Foundation continues to schedule on-base events to reach the men and women of the military with this important message. The next scheduled events are two forums at the Naval Submarine Base in Kings Bay, Georgia, on June 13, 2006.

These events give us valuable insight into what issues are important to the members of the military. In both Okinawa and Yokosuka, there was a great deal of interest in predatory lending and how to dig out of debt. There is a clear lack of knowledge about 529 plans, and it was also clear from the audience questions that the Thrift Savings Plan (TSP) was not well understood. NASD plans to create additional content on the SaveAndInvest.org Web Site to clearly and concisely explain the TSP to military personnel.

Our Partners

The NASD Foundation joined forces with the SEC, the National Military Family Association, the Association for Financial Counseling and Planning Education, the InCharge Education Foundation, the National Endowment for Financial Education, the American Savings Education Council, CinHouse.com and the Consumer Federation of America to develop programs, provide training, and distribute information and resources to the military community.

Future Plans and Programming

Through a combination of its own initiatives and partner programs funded by foundation grants, the NASD Foundation will bring the financial education community together with the goals of empowering individuals to learn more in less time, helping organizations work together on new and existing initiatives, and establishing more coordinated and uniform financial education programs. Specific programs will include:

- a financial education e-learning game specifically designed for servicemembers and their families;
- educational toolkits for trainers, offering multiple levels of personal financial information; and
- the expansion of Military Saves, a national program designed by the Consumer Federation of America to encourage servicemembers and their families to save and build wealth.

In order to ensure the Military Financial Education Program's effectiveness, the NASD Foundation plans to conduct a follow-up survey of servicemembers and their families to evaluate the effectiveness of the campaign. In addition, the NASD Foundation will report on changes within DOD, service-specific military command, and other partners to address the importance of financial readiness. We will also measure the demand for financial and investor education materials related to the campaign.

Conclusion

Thank you for giving us the opportunity to testify on these important topics and for your important work on this issue. America's men and women in uniform deserve honesty and integrity from those who sell them financial products. NASD will continue its work to protect all investors, including those in our nation's military.