

# NASD Data Now A Click Away on the World Wide Web

*Published In Massachusetts Bar Association Section Review July, 1999*

Massachusetts' enactment of the Prudent Investor Act (1998 Acts and Resolves c. 398, codified at G.L. c. 203C, §§ 5 1-11 (approved Dec. 4, 1998)) gave trustees a welcome assurance that they had power to flexibly manage the assets under their control as a single portfolio, rather than on an investment- by-investment basis, G.L. c. 203C, 5 3. It did, not, of course, relieve fiduciaries of their duty to "exercise reasonable care, skill and caution," G.L. c. 203C, § 3(a). Trustees' standard of care has changed with the evolution of information technologies from the time modern financial accounting was developed to the present. The availability of instant data on both financial instruments and financial service providers through the Internet can, and will, impose new responsibilities on trustees —especially those non-institutional trustees who take direct responsibility for management of their beneficiaries' financial assets.

Newly-enacted G.L. c. 203C, §10(a) expressly authorizes Massachusetts trustees to delegate investment and management functions, provided they "exercise reasonable skill and caution in," among other things, "selecting an agent." In many cases, lay trustees may choose to employ either a securities broker or a registered investment adviser associated with a securities broker, to serve as both a custodian of assets and an investment adviser. Fiduciaries always had the obligation to investigate the bona fides of brokers and advisers even before the Prudent Investor Act expressly permitted their engagement. The development of both computer databases and, more recently, the ability to access such databases interactively over the Internet, makes it far easier to conduct such a review today. The existence of such resources may mandate their use by trustees when they choose to employ the services of professional managers.

Since 1981, the National Association of Securities Dealers (one of the two principal self-regulatory organizations in the brokerage industry) has operated (on behalf of state securities regulators), a Central Registration Depository~ The CRD contains personnel and disciplinary records for all individuals licensed as registered representative to sell securities in the United States. Stockbrokers and their employers must report to CRD "promptly" after their occurrences:

- final disciplinary actions (relating to securities or commodities businesses) that have been taken by NASD Regulation and other self-regulatory organizations (e.g., the New York Stock Exchange), or by federal, state and foreign securities agencies
- civil judgments and arbitration decisions in securities and commodities disputes involving public customers
- criminal convictions, informations and indictments

- settlements of \$10,000 or more among the parties to arbitrations, civil suits, and customer complaints involving securities and commodities transactions
- pending industry disciplinary actions that relate to securities or commodities business
- pending arbitrations and civil proceedings involving securities or commodities transactions
- pending written complaints alleging sales practice violations seeking damages of \$5,000 or more
- employment terminations after allegations were made involving violations of investment related statutes or rules, fraud, theft or (on the part of managers) failure to supervise investment-related activities
- existence of outstanding judgments and liens and whether an individual broker has sought bankruptcy protection within the previous 10 years

CRD was inaugurated to provide state regulators with a central data bank. However, investors and other members of the public are also eligible to receive information. The increasing ease of access to this material imposes new duties on fiduciaries that either manage funds or delegate the management of funds to others.

Between 1987 and 1997, CRD data on a broker's disciplinary history was available only through written request, or, more recently, a roll-free telephone line, (800) 289- 9999, maintained by the NASD. Since 1997, however, the NASD has eased access to CRD information by making it available through the World Wide Web site of NASD Regulation Inc., the subsidiary that currently operates CRD. Visitors to [www.nasdr.com/1000.asp](http://www.nasdr.com/1000.asp) can look up a broker's name and obtain information such as his or her current and former employers and the states in which the broker is licensed to do business. More importantly, the site will indicate whether or not the broker's record contains reports of customer complaints or disciplinary action.

Detailed records are not yet available through the Web (pending resolution of privacy-related questions, including disclosure of non-securities related criminal convictions). Nonetheless, requests for Full disclosure of such records (via either postal mail or e-mail) may be transmitted through the NASD Web site. The NASD does not charge individual investors for copies of such reports. Turn-around on such requests through e-mail is now often less than one week.

Full records will identify the existence of customer complaints (including complaints that were either withdrawn or settled), results of arbitration cases in which the broker was a party and disciplinary actions taken against the broker. The NASD report can then be used as a means of obtaining copies of arbitration awards or disciplinary decisions available in the public files of either the NASD or other self-regulatory organizations, the SEC, or state agencies. There is a nominal fee for copies of arbitration decisions; details of SEC and NASD actions against individual brokers can often be found through the NASD Regulation and SEC ([www.sec.gov](http://www.sec.gov)) World Wide Web sites.

The availability of more information about those to whom a trustee may delegate investment responsibilities implicates a trustee's duty "to exercise a sound discretion, and to be enlightened by observance *Springfield Safe Dep. & Trust Co. v. First Unitarian Soc.* 293 Mass. 480, 485, 200 N.E. 541, 545 (1936). The Prudent Investor Act may make explicit a fiduciary's right to employ investment professionals. The new law's direction that a trustee must employ "reasonable care, skill and caution" leaves little doubt that the failure to review publicly available information concerning investment professionals entrusted with trust assets may expose the trustee to personal liability in the event of defalcation or mismanagement. *Cf. Barker v. Am. Mobil Power Corp.* 64 F.3d 1397, 1403 (9th Cir. 1995) (ERISA trustee who fails to investigate apparent misconduct by plan administrator may be liable for breach of fiduciary duty under ERISA 404, 29 U.S.C. 1104), Trustees who are not investment professionals—and the attorneys who advise them—must utilize Internet-based information on the background of the advisors they propose to employ. The routine review of such information either has become, or is about to become, a component of a prudent fiduciary's duty of care to beneficiaries.