

In the Matters of SPEAR & STAFF, INCORPORATED, 8 Babson Park Avenue, Babson Park, Wellesley Hills, Massachusetts, ROGER E. SPEAR, 8 Babson Park Avenue, Babson Park, Wellesley Hills, Massachusetts

File Nos. 801-83, 801-2233

**SECURITIES AND EXCHANGE COMMISSION**

**INVESTMENT ADVISORS ACT OF 1940, Section 203(d), Release No. 188**

March 25, 1965

**ACTION: INVESTMENT ADVISER REGISTRATION**

**Grounds for Disciplinary Action**

**Deceptive Advertisements**

Where registered investment adviser's advertisements implied that it possessed ability to select securities certain to increase in price substantially and rapidly and did not adequately disclose uncertainties inherent in forecasting security prices and, referred to certain past recommendations without giving information as to those and other recommendations by registrant or including cautionary legend as required by Rule 206(4)-1(a) under Investment Advisers Act of 1940, held, willful violations of anti-fraud provisions of Act and of Rule.

**Public Interest**

Where registered investment adviser had used misleading advertising material in violation of Investment Advisers Act of 1940, but it and its president had been engaged in number of investment advisory activities for many years, violations related to one aspect of such activities, and record showed efforts to comply with statutory standards, held, acceptance of offer of settlement by which registrant undertook to refrain from advertising for new subscribers for 90 days and to institute new controls aimed at prevention of future violations was appropriate in the public interest under all the circumstances.

**COUNSEL:**

**APPEARANCES:**

Edward P. Delaney and Willis L. Riccio, of the Boston Regional Office of the Commission, Frederick Moss and Sven L. Johanson, for the Division of Trading and Markets.

Roland A. Cormier, of Ely, Bartlett, Brown & Proctor, for respondents.

**TEXT:**

**FINDINGS AND OPINION OF THE COMMISSION**

We heretofore issued an order accepting an offer of settlement submitted in these proceedings by respondents Spear and Staff, Inc. ("registrant") and Roger E. Spear. n1 In that order we found, on the basis of the offer and a stipulation of facts accompanying it, that the registrant willfully violated Sections 206(2) and 206(4) of the Investment Advisers Act of 1940 ("Act") as well as Rule 206(4)-1 thereunder, n2 and that such violations were aided and abetted by Roger E. Spear ("Spear"), registrant's president and majority stockholder. The order directed, as provided in the offer of settlement, that registrant refrain for 90 days from advertising for new subscribers to its publications and that during that period registrant should undertake to establish new controls for the purpose of preventing future violations of the Act. We set forth below our findings and opinion with respect to the issues in the case.

**Registrant and its Advertisements**

Registrant was formed in 1948 to succeed to an investment advisory business which Spear had conducted since 1940. Spear is registrant's president and majority stockholder and exercises general supervision over all of its activities. n3 A major activity of registrant, which also acts as an investment manager for others, is the sale to subscribers of three market letters: Spear Market and Group Trend Letter, a weekly which discusses current economic conditions and makes recommendations concerning

securities; Science and Electronic Investment Letter, a bi-weekly which discusses developments in the science and electronics industries and makes recommendations as to securities in those industries; and Special Situation Reports, a monthly which advises with respect to securities selected by registrant as having special features. n4 To induce persons to enter or renew subscriptions for these services, registrant engaged in a large-scale program of direct mail and newspaper advertising. n5 It is with that advertising that these proceedings are concerned.

The record includes a large number of advertisements which were used by registrant beginning January 1, 1962. Pervading and dominating this literature, which was couched in enthusiastic and dramatic language, was the insistent implication that registrant possessed the ability to select stocks that were certain to appreciate in price quickly and substantially, and that a certain road to riches was at hand for those who availed themselves of registrant's guidance. Caution and conservatism were scorned as attributes of people who "are still thinking small." n6 Of such people registrant said: "They are mentally back in the 19th Century, worrying about a 3%, 5% or 8% annual return on their money. They are missing out on the very few but very rewarding opportunities to earn 100%, 200% or even more profit in one-to-two years." . . . "And there is no reason why sophisticated investors should be satisfied with 5% or 10% return on their money, when certain Special Situations are rewarding others with gains of 50%, 100% and more, regardless of the action of the rest of the market."

Registrant's most extensively used advertisement dealt with "special situation investing." It defined a special situation as "a security whose primary characteristic is its 'built-in' capacity to bring extraordinarily large capital gains," and it described special situation investing as "A BRILLIANT AND PROFITABLE INVESTMENT CONCEPT . . . a proven, highly professional approach to making money in the stock market . . . that is both bold and simple, yet technically sound, intrinsically safe, and completely practical." The advertisement stated that Wall Street experts had for years virtually monopolized that "profit-making market approach, using it with remarkable success," but that "Now" the chance was open to the subscriber to add to his wealth through special situations and that they could bring him "the greatest profit at the smallest risks." Another frequently used advertisement asked the prospective subscriber whether his ambition was to double his money in perhaps 12 to 24 months and urged that if it was he should learn about special situation investing from registrant right away.

A technique used extensively in registrant's literature was to recount outstanding success stories and attribute the success of the selected individuals to investments in "special situations," thereby furthering the impression that registrant was able to uncover for its subscribers opportunities for outstanding profits comparable to those which the described individuals had been able to realize. Thus, advertisements directed to those "tired of working so hard to squeeze out \$1000 or only \$100 profits from stocks," told of three men who had applied "certain investing principles" to lift themselves "out of the muck of poverty up into the golden sunlight of wealth, power and fame" and became millionaires by detecting and exploiting "special situations." The three men were Cornelius Vanderbilt, who was stated to have begun his financial ascent by investing a borrowed \$1,000 in a barge of his own; Andrew Carnegie, whose rise to riches was attributed to a \$217.50 investment made in a "special situation" with borrowed funds; and John D. Rockefeller, whose career was briefly sketched and whose first investment in oil was described as "a shrewd special situation investment." n7 Other advertisements described the career of a teacher who had never earned more than \$6,000 a year but who nevertheless amassed \$1,000,000 by successful operations in the depressed securities markets of the 1930's, and they attributed such success to the teacher's ability to select "special situations" and spoke of registrant's own abilities along the same line. n7

The over-all impression of certain, substantial, and quick profits through the utilization of registrant's advisory services was additionally fostered by the excessive optimism with which registrant described its securities selections. For example, various of the advertisements referred to unnamed stock selections made by registrant's staff which were most likely to show large and quick profits. One stated that the selections included a "Young Stock That May Be A Pay-For-Your-Grandson's College Education Investment." Another spoke of a forthcoming report by registrant in which three very low-priced science stocks that could offer big profits were to be described, and not-too-modestly said of the report that "its every word is pure gold." Still another told the prospective subscriber that registrant offered "a plan aimed at helping you make an extra \$300 or \$3,000 - and perhaps raise your standard of living." Several letters to prospective subscribers announced that registrant had come across a "Special Situation profit opportunity which appears to be so exceptional that we have difficulty in believing our

good fortune in discovering it" and as to which registrant had "projected a profit objective of 75% within 10 months." Each of the letters stated that it was "the last opportunity we can give you to receive this recommendation with your membership."

Registrant's advertisements also contained references to various securities that had experienced considerable price appreciation. Such references were closely coupled to registrant's flamboyant self-laudatory claims, and their effect was to imply that the stocks recommended in registrant's advisory letters would duplicate the record of the securities referred to.

In our opinion, registrant's advertisements were calculated to arouse, in an excessive and unwarranted manner, illusory hopes of immediate and substantial profit, and were violative of the Act's anti-fraud provisions and of Rule 206(4)-1(a) thereunder. They were deceptive and misleading in their over-all effect even though it might be argued that when narrowly and literally read, no single statement of a material fact was false. n8 In appraising advertisements such as those now before us we do not look only to the effect that they might have had on careful and analytical persons. We look also to their possible impact on those unskilled and unsophisticated in investment matters.

And Rule 206(4)-1(a)(5) prohibits both advertisements that contain any untrue statement of material fact and those that are otherwise false and misleading.

By the securities acts Congress sought to protect "those who do not know . . . from the over-reaching of those who do." n9 To attain that objective, persons engaged in the securities business must be held to rigorous standards of full and fair disclosure in their dealings with investors. The rendition of investment advice is an integral part of the securities business, and the Act evidences Congressional recognition of that fact and of the need to protect those who seek such advice. n10 In passing upon the propriety of securities selling techniques we have repeatedly held that lax merchandising standards epitomized by such terms as "puffing" are antithetical to the anti-fraud provisions of the securities statutes. n11 Similarly high standards of truthfulness and disclosure must also govern the propriety and legality of investment advisers' efforts to induce others to purchase their services. n12 They are particularly applicable to advertisements of the type involved here which by their tenor show that they were designed to appeal to people who were anxious to secure quick profits and were not especially sophisticated in security analysis. Many such persons are either unaware of or prone to overlook the limitations and the uncertainties necessarily inherent in any attempt to forecast stock prices. They tend to be unduly influenced by advertisements representing or implying that the advertiser can make profitable forecasts and to subscribe to the advertiser's advisory services in reliance on them. n13

Appraised in the light of the foregoing considerations and standards, registrant's advertisements were clearly deceptive. They obscured and misleadingly minimized the numerous uncertainties and imponderables inherent in any attempt to forecast security prices. There were occasional caveats, but they were unobtrusively worded and placed, being generally preceded and followed by highly optimistic statements that off-set any cautionary effect. Illustrative was a sentence which read: "Like all stocks, these situations often call for calculated risks." That sentence was preceded by three pages emphasizing the large profits that could be made by those who read and heeded registrant's Special Situation Reports, and was countered immediately by the next sentence which again spoke of the "unusual profits" that could be made with Special Situation stocks and the almost exclusive investment in such stocks by "knowledgeable investors . . . to build their capital."

Another advertisement, after describing the outstanding increase in the price of Zenith Radio Corporation stock made the following ostensibly sobering qualification "But by and large, experience has taught us that it is more prudent to set modest goals for special situations . . . perhaps a 100% profit in 18 months. Then, if developments turn out more favorably than we conservatively anticipated, and if a stock turned out to be a long-term fortune-builder (of the nature of Zenith), then your surprise would be a pleasant one. Far better, we believe, to try and set modest goals and exceed them occasionally, than to set unrealistic goals and fall short of them continuously." This language, rather than modifying registrant's optimism, suggested to the reader that the "modest" and "conservative" goal of a 100% profit in 18 months was surely attainable under registrant's "prudent" securities selections. n14 In our view registrant's optimism was so extravagant that even an explicit caveat could not have brought this advertisement up to the statutory standard. n15 Nor did registrant adequately qualify its glowing recitals of extraordinary past successes by selected individuals and stocks so as to place them in a realistic

perspective. n16

Registrant, aided and abetted by Spear, also willfully violated Rule 206(4)-1(a)(2) n17 by one advertisement which referred to securities that it had previously recommended, and by various "Progress Reports" which registrant had distributed to subscribers to its Special Situation Reports. These materials contained neither a list of all of registrant's recommendations for at least one year preceding nor the cautionary legend prescribed by that Rule. n18 Although the advertisement in question did not expressly refer to the fact that registrant had recommended the securities discussed, it went on to say that registrant wished it could state that its staff had come up with "another stock which we are sure will be another winner." The use of the word "another" indicated that the securities discussed had been recommended by registrant, and we accordingly view the advertisement as one making reference to past recommendations within the meaning of Rule 206(4)-1(a)(2) and therefore subject to the requirements of that Rule. The "Progress Reports" listed only those securities which had been the subject first of "buy" and later of "sell" recommendations by registrant, and did not include all securities recommended by registrant. The information in the Progress Reports, which consisted of a chart showing the name of the security, the prices at the time of the recommendations to purchase and to sell and the percentage gain or loss which would have resulted, was not of a kind to aid the subscribers in making any current investment decisions. We think it apparent that the Reports' primary, if not sole, purpose was to induce those to whom they were sent to renew their subscriptions. Accordingly they were advertisements within the meaning of the Rule and had to comply with the specific requirements of subdivision (a)(2). n19

## Conclusions

Registrant's sensational advertisements featuring the get-rich-quick theme were incompatible with responsible methods of obtaining clients for investment advisory services. Advertisements of this kind have a substantial adverse effect on the public interest. Not only do they tend to mislead and deceive investors, they also tend to debase the standards of the investment advisory industry by creating a competitive environment that tempts advisers to vie with each other in making unsupportable claims to prophetic insight. n20 Our Special Study of Securities Markets found that "The impact of such advertising is apparently considerable and thus a cause for concern." n21

We determined to accept respondents' settlement offer despite the seriousness with which we viewed the violations in this case because our review of the record led us to concur with our staff's conclusion that under the circumstances the public interest was adequately served by the sanction proposed under the offer. In reaching our decision we took into account that this is one of the first administrative proceedings in which we have dealt with the question of improper investment advisory advertising material, that respondents have been in the investment advisory business for many years, that their violations related to one aspect of their diversified advisory activities, and the indications in the record that they had during the latter portion of the period relevant to these proceedings attempted to conform registrant's advertisements to the statutory standards. Registrant voluntarily discontinued all newspaper advertising in April of 1962, after members of our staff had informally advised it that they were of the opinion that its newspaper advertisements were violative of the Act, and its direct mail materials during the later portion of 1962 and in 1963 were more moderate in tone and of a higher caliber than those of early and mid-1962.

In light of those factors we also gave weight to registrant's undertaking to further reexamine its past practices with a view to the prevention of future violations. However, the relative leniency of the sanction that we impose in this case should not be misconstrued. In light of the admonitions of this opinion we shall be disposed to deal more severely with any future instances of false and misleading advertising by investment advisers.

By the Commission (Commissioners WOODSIDE, OWENS, BUDGE and WHEAT), Chairman COHEN absent and not participating.

## Footnotes

n1 Investment Advisers Act Release No. 174 (July 14, 1964).

n2 Section 206(2) forbids an investment adviser from engaging in "any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." Section 206(4) prohibits investment advisers from engaging "in any act, practice or course of business which is fraudulent, deceptive or manipulative." Rule 206(4)-1 deals with advertisements, and subdivision (a)(5) thereof provides that any advertisement "which contains any untrue statement of a material fact, or which is otherwise false or misleading" is fraudulent under that Section.

n3 Spear, who is himself registered as an investment adviser, is also the president and controlling stockholder of Oil Statistics Co., a registered corporate investment adviser with which he has been associated since 1924. He also publishes, with the assistance of registrant's staff, a syndicated newspaper column on the stock market which he began in 1960.

n4 As of January 1962 registrant had a staff of 84, and the three market letters had a total of over 17,000 subscribers. In August of 1963 registrant began the publication of a fourth market letter called Computer Stock Analysis Technique, a bi-weekly.

n5 Registrant advertised frequently in the New York Times, and some of its direct mail advertising went to as many as 150,000 people. Four of registrant's employees devoted themselves to its advertising program.

n6 All of the quotations from registrant's advertisements that appear in this opinion retain the original punctuation, underscoring, italics and capitalization.

n7 Occasional references were also made to the elder J. Pierpont Morgan and to "Bet a million" John W. Gates.

n8 Fraud within the meaning of the Act can be established without proof of false statements. *S.E.C. v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 185-195 (1963).

n9 *Charles Hughes & Co. v. S.E.C.*, 139 F.2d 434, 437 (C.A. 2, 1943), cert. denied 321 U.S. 786. See also *Norris & Hirshberg v. S.E.C.*, 177 F.2d 228, 233 (C.A.D.C., 1949), cert. denied 333 U.S. 867 ("The investing and usually naive public needs special protection in this specialized field."). Cf. *F.T.C. v. Standard Education Society*, 302 U.S. 112, 116 (1937) ("Laws are made to protect the trusting as well as the suspicious."); *Donaldson v. Read Magazine*, 333 U.S. 178, 185-189 (1948); *F.T.C. v. Sterling Drug, Inc.*, 317 F.2d 669, 674 (C.A. 2, 1963); *Parker Pen Co. v. F.T.C.*, 159 F.2d 509, 511 (C.A. 7, 1946); *Charles of the Ritz Dist. Corp. v. F.T.C.*, 143 F.2d 676, 679-680 (C.A. 2, 1944) ("The important criterion is the net impression which the advertisement is likely to make upon the general populace"); *Aronberg v. F.T.C.*, 132 F.2d 165, 167 (C.A. 7, 1942); *The Private Investment Fund for Government Personnel*, 37 S.E.C. 484, 487-488 (1957); *National Securities & Research Corporation*, 12 S.E.C. 167, 171-172 (1942).

n10 See *S.E.C. v. Capital Gains Research Bureau*, supra, at pp. 186-192. It was judicially recognized long prior to the Act that investment advisers stand in a fiduciary relation to their clients. See *Ridgely v. Keane*, 134 App. Div. 647, 119 N.Y.S. 451, 453 (1909). The Act reflects the existence of such relationship. See *S.E.C. v. Capital Gains Research Bureau, Inc.*, supra, at 194-195; *Arleen W. Hughes*, 27 S.E.C. 629, 635-638 (1948), aff'd sub nom. *Hughes v. S.E.C.*, 174 F.2d 969 (C.A.D.C., 1949); *Frank Payson Todd*, 40 S.E.C. 303, 307 (1961).

n11 See e.g., *Mac Robbins & Co.*, Securities Exchange Act Release No. 6846, p. 4 (July 11, 1962), aff'd sub nom. *Berko v. S.E.C.*, 316 F.2d 137 (C.A. 2, 1963); *Alexander Reid & Co., Inc.*, 40 S.E.C. 986, 989-991 (1962); *Leonard Burton Corporation*, 39 S.E.C. 211, 214 (1959); *Batkin & Co.*, 38 S.E.C. 446, 449 (1958).

n12 As noted, Section 206 of the Act bars conduct that defrauds or deceives "any client or prospective client," and we have held that the solicitation of clients is part of the activity of an investment adviser. *Ralph Seward Seipel*, 38 S.E.C. 256, 257 (1958).

n13 See REPORT OF THE SPECIAL STUDY OF SECURITIES MARKETS OF THE SECURITIES AND EXCHANGE COMMISSION, H.R. Doc. No. 95, Pt. 1, 88th Cong., 1st Sess. (1963) p. 368 [hereinafter

cited as "SPECIAL STUDY REPORT."]

n14 Cf. Doman Helicopters, Inc., Securities Act Release No. 4594, p. 5 (March 27, 1963).

n15 Cf. Advanced Research Associates, Inc., Securities Act Release No. 4630, Securities Exchange Act Release No. 7117, p. 5 (August 16, 1963).

n16 See Irving Grubman, 40 S.E.C. 671, 672-673 (1961); G.J. Mitchell Co., 40 S.E.C. 409, 413 (1961); Stratford Securities Co., Inc., 39 S.E.C. 826, 828 (1960); The Whitehall Corporation, 38 S.E.C. 259, 266-267 (1958); American Republic Investors, Inc., 37 S.E.C. 287, 290 (1957).

n17 Rule 206(4)-1(a)(2) provides that it is fraudulent within the meaning of Section 206(4) for any investment adviser to distribute any advertisement "which refers, directly or indirectly, to past specific recommendations of such investment adviser which were or would have been profitable to any person," but permits advertisements that set out (or offer to furnish a list of) all of the adviser's recommendations within the immediately preceding period of not less than one year if such advertisements (or such list, if it is furnished separately) "(A) state the name of each such security recommended, the date and nature of each such recommendation (e.g., whether to buy, sell or hold), the market price at that time, the price at which the recommendation was to be acted upon, and the market price of each such security as of the most recent practicable date, and (B) contain the following cautionary legend on the first page thereof in print or type as large as the largest print or type used in the body or text thereof: 'it should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list.'"

n18 It may be noted that under the Rule an advertisement which contains a list of only a portion of the investment adviser's past recommendations would not be cured by an offer in the same advertisement to furnish a complete list upon request.

n19 Moreover, it may be noted that even aside from the specific prohibitions of Rule 206(4)-1(a)(2) applicable to advertisements, a list showing only gains and losses which would have been realized by following an adviser's past buy-and-sell recommendations and does not disclose the effect of other recommendations that the adviser has not seen fit to close out prior to the publication of the list, may be a deceptive guide to an investment adviser's over-all performance record.

n20 See SPECIAL STUDY REPORT, *supra*, 367-8.

n21 *Ibid.*