

**MEMO# 3501**

February 7, 1992

## **COMPLIANCE WITH NEW SIGNATURE GUARANTEE RULE**

February 7, 1992 TO: SEC RULES MEMBERS NO. 6-92 OPERATIONS MEMBERS NO. 5-92  
TRANSFER AGENT ADVISORY COMMITTEE NO. 7-92 RE: COMPLIANCE WITH NEW SIGNATURE  
GUARANTEE RULE \_\_\_\_\_ A meeting of  
the Institute's Transfer Agent Advisory Committee was held on Friday, January 31, 1992 in  
Washington to identify problems and discuss compliance options in connection with new  
Rule 17Ad-15 under the Securities Exchange Act of 1934 regarding acceptance of signature  
guarantees. The rule is effective February 24, 1992. (For a copy of the final rule, see ICI  
Memorandum to SEC Rules Members No. 2-92, Operations Members No. 2-92, and Transfer  
Agent Advisory Committee No. 2-92, dated January 17, 1992.) This memorandum provides  
a synopsis of the rule, summarizes the discussion at the January 31 meeting and provides  
additional information that may be helpful to ICI members preparing to comply with the  
rule. SYNOPSIS OF RULE WRITTEN STANDARDS AND PROCEDURES The rule requires  
registered transfer agents to establish written standards and procedures for the acceptance  
of signature guarantees from "eligible guarantor institutions," defined in the rule to include  
banks, brokers, dealers, credit unions, securities exchanges and associations, clearing  
agencies and savings associations. The standards, as written or applied, may not treat  
different classes of eligible guarantor institutions inequitably. A transfer agent generally  
may not reject a signature guarantee from an eligible guarantor unless the guarantor does  
not satisfy the transfer agent's written standards or procedures. -2- SIGNATURE  
GUARANTEE PROGRAMS The rule which permits transfer agents to incorporate in their  
written standards that they will (1) accept guarantees from eligible guarantors who  
participate in a signature guarantee program or (2) reject guarantees from eligible  
guarantors who are not participants in a signature guarantee program. However, transfer  
agents electing to accept guarantees only from guarantors who are participants in a  
signature guarantee program may not, for a six month transition period from the date their  
written standards are established or revised accordingly, reject guarantees from eligible  
guarantors because the guarantor is a non-participant. "Signature guarantee program" is  
defined in the rule as one whose terms and conditions the transfer agent determines to  
facilitate the equitable treatment of guarantors and to provide adequate protection against  
risk of loss or the issuance of unauthorized guarantees. EXCLUSIONS The rule provides that  
transfer agents are not prohibited from rejecting certain items for reasons unrelated to  
acceptance of the guarantor institution, for example, where the transfer agent suspects  
forgery or believes that the transaction would otherwise be wrongful. Also excluded are  
items rejected because the person acting on behalf of the guarantor is not authorized  
(provided the transfer agent keeps a list of authorized signatories) or where the guarantor  
is a broker or dealer and is neither a member of a clearing corporation nor maintains net  
capital of at least \$100,000. NOTIFICATION OF REJECTIONS Transfer agents must notify

guarantors and presentors of any rejections and the reasons therefor within two days of any rejections that are based on a determination that the guarantor does not meet the written standards of the transfer agent. Notification to the presenter may be accomplished by making the rejected item available to the presenter. Notification to the guarantor may be accomplished by telephone, fax or mail. RECORDKEEPING Every transfer must maintain a copy of the standards and procedures in an easily accessible place and make a copy available to any requesting person within three days of the request. Transfer agents must also maintain, for a period of three years following a rejection, a record of transfers rejected, including the reason for the rejection, who the guarantor was and whether the guarantor failed to meet the transfer agent's written standards.

-3- SUMMARY OF MEETING DISCUSSION WRITTEN STANDARDS AND PROCEDURES Options for complying with the written standards and procedures requirement were discussed at length. The available options appear to be as follows: 1. Accept from all eligible guarantors. 2. Accept from eligible guarantors meeting written standards. 3. Accept from eligible guarantors meeting written standards and participants in approved signature guarantee program(s). 4. Accept only from participants in approved signature guarantee program(s). By the end of the meeting, virtually all attendees agreed that the only realistic alternative at this time is to accept signature guarantees from all eligible guarantor institutions and indicated they would expect to establish their written standards accordingly. Options 2 and 3 above were generally regarded as not realistic at this time because transfer agents do not have the resources to apply financial creditworthiness criteria, on an ad hoc basis, to every eligible guarantor providing a signature guarantee. Option 4 was viewed by most as not realistic at this time because there currently is only one signature guarantee program in existence (Securities Transfer Agents Medallion Program or "STAMP") and it is not expected to be operational until February 24, 1992, the effective date of the rule. Moreover, even if STAMP finds acceptance among the guarantor community, it will take time for a sufficient number of guarantors to enter the program to make this option viable for transfer agents. Fund groups that have trustee approval to waive signature guarantees for all but a relatively limited set of transactions (for example, where the dollar threshold beneath which guarantees are not required is relatively high), may consider the application of financial criteria to individual guarantors a feasible activity.

CERTAIN CREDIT UNIONS The group considered an issue briefly discussed in the SEC's adopting release regarding the authority of state chartered credit unions to issue signature guarantees. While the definition of "eligible guarantor institution" in the rule includes, in effect, all credit unions, the release qualifies the -4- definition to guarantors that are "authorized" to provide signature guarantees. While it is believed that most state credit unions are probably authorized under state law to provide guarantees as an "incidental power" or "goodwill service," there is no general authority that can be cited as in the case of federal credit unions and the other classes of guarantor institutions. The Institute is investigating whether state chartered credit unions without authority to provide signature guarantees can be easily identified and listed. In the meantime, the release permits transfer agents to require assurance from guarantors of their signature guarantee authority to the extent it is not a matter of general knowledge. Therefore, it appears that transfer agents may include in their written standards and procedures a requirement that state chartered credit unions furnish a citation of their authority to provide signature guarantees without running afoul of the rule's "inequitable treatment" prohibition.

MODEL WRITTEN STANDARDS The Securities Transfer Association (STA) is currently preparing a model set of written standards for its membership and has agreed to make this document available to the Institute for distribution to the ICI membership. The STA model is expected to be completed and available within a week. Participants at the Institute's January 31 meeting were requested to provide copies of their written standards to the Institute when they are completed. The ICI staff will then be able to

advise members as to the development of any generally accepted approaches and associated language. COMMUNICATION OF WRITTEN STANDARDS The group addressed the question of whether prospectuses would need to be stickered on or before February 24, 1992 to reflect the written standards. The consensus was that stickering would not be necessary and virtually all participants indicated they would expect to provide prospectus disclosure about their transfer agents' written standards in their funds' next regular amendments. It was noted that shareholder servicing staff will need to be educated about any new or changed standards and procedures to be able to apply the requirements and explain them to shareholders. -5- MODIFICATION OF WRITTEN STANDARDS There appears to be nothing prohibiting a transfer agent from changing its written standards and procedures whenever it wishes (until prospectuses are revised to reflect the established standards). Therefore, transfer agents may consider fine-tuning their standards and procedures as necessary or desired as experience is gained under the rule. RECORD RETENTION The rule is not completely clear on which rejections must be maintained in a separate record for the required three year period. There is a question as to whether the requirement relates only to those rejections caused by failure of the guarantor to meet the transfer agent's standards, or all rejected items for any reason whether or not signature guarantees were required, or something in between. Based on informal discussions with the SEC staff, the staff preliminarily seems to favor an interpretation requiring that transfer agents maintain a record of every rejected item for which a signature guarantee was required, irrespective of the reason for the rejection. STAMP STAMP is a program developed under the sponsorship of the STA that will enable eligible guarantors to obtain surety bonds in amounts ranging from \$100,000 to \$1 million to satisfy claims of transfer agents where guarantors cannot respond. In addition, STA will obtain a \$10 million liability insurance policy to satisfy claims in excess of a guarantor's surety bond limit. STA expects to increase the policy limits to the \$50-\$100 million range within five years. STAMP will be governed by an independent board of individuals representing financial service groups. The program will be administered by Kemark Financial Services. Kemark expects to begin disseminating STAMP marketing materials to the guarantor community within the next week. The Institute will obtain copies of STAMP materials for distribution to the ICI membership for your information and review along with the STA model written standards as soon as they become available. \*\*\*\*\* We will keep you informed of significant developments in connection with implementation of this rule and we will forward any relevant materials and information to you as they become available. Donald J. Boteler Assistant Vice President- Operations