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CONFIDENTIAL

Mr. J. William O'Reilly

NEW YORK STOCK EXCHANGE

MEMORANDUM

September 28, 1971

TO: Mr. Robert W. Haack

FROM: William C. Freund

SUBJECT: Working Committee on a National Securities Exchange

You asked that I outline the problems discussed and the conclusions reached by the Committee so far:

1. There is agreement on broad general principles only. On specifics, each exchange is attempting to retain its competitive advantages.

2. The broad principles agreed to are as follows:

   a. A centralized securities market is not one geographic location or one marketplace but a system or a communications network.

   b. Autonomously-administered market centers, consisting of the present exchanges, are to be retained.

   c. An appropriate vehicle must be created for purposes of coordination. The nature of the coordinating body, its powers over the autonomously-administered market centers, and its other characteristics remain to be defined.

   d. There is to be prompt and complete disclosure of transactions in all market centers through a composite tape.

   e. The system will provide for competing market makers and broad dissemination of bids and offers. For example, the best bid for G.M. may be in Chicago; the best offer in Philadelphia. Customers would be assured of the "best" price through full disclosure of competing quotes.

   f. The autonomously-administered market centers will also provide a vehicle for competition in terms of administrative and technological innovations.

3. The operational characteristics of the system have not yet been defined even conceptually. Some difficult questions now under discussion are:

a. Access. The system must give broker-dealers who are members of one market center access to another. There has been discussion of an access rate of, say 50%, although this figure was used illustratively. Some exchanges, e.g., Pacific Coast, see nothing wrong with regular-way reciprocity as the form of access. As its spokesman put it, "Regionals now provide access to the NYSE for a membership fee of $25,000. We cannot easily give that up." Regionals will not accept a ban on reciprocity unless that ban is accompanied by assurance that access to the NYSE will be provided in such a way as to promote the incentive to membership on regional exchanges.

b. Uniform minimum rules. It was agreed in principle that minimum and, to the extent possible, uniform rules and regulations should be adopted and enforced on all exchanges with respect to trading and dealer activities on the floor of the various exchanges. However, on specifics, e.g., uniform capital requirements for members and specialists, there is as yet no agreement. Also, the whole issue of uniform regulation of specialist activities has not been discussed.

c. Institutional membership. The desirability of uniform membership rules has been acknowledged. All exchanges, except Philadelphia, seem to favor a ban on institutional membership with the latter adamantly rejecting that proposal. Committee members agree that common membership rules must be adopted lest membership requirements on all exchanges fall to the lowest common denominator. It is also recognized that if institutions continue to enjoy membership on Philadelphia, they would automatically have access to all other market centers participating in the system. The issue of institutional membership will probably have to be resolved by the SEC, although the Pacific Coast Stock Exchange pointed out that existing competition among markets on institutional membership may deprive the SEC of the time to act.

There was also some discussion concerning the desirability of adopting the Midwest Rule on primary purpose, or some variant thereof. This rule requires that broker-dealer subsidiaries receive at least 50% of their income from conducting a broad public brokerage business. Although this rule does not admit institutions, it allows membership to bona-fide brokerage subsidiaries of firms engaged in other lines of business.

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