10/16/72

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

MEMORANDUM

TO: Officers and Managers of Member Firms and Branch Offices and NASDAQ Subscriber Representatives

One of the products emanating from the joint efforts this year of the NASD and the National Security Traders' Association to inform and educate the public about the over-the-counter market and the NASDAQ system is a new $13\frac{1}{2}$ minute, color motion picture entitled 'The Electronic Stock Market".

Prints of this 16mm film are now available on a free loan basis to NASD members and other interested individuals from any Association District Office and the NASDAQ Office at 17 Battery Place, New York, New York 10004.

This motion picture has been especially produced for the membership to use in firm-sponsored investment seminars, local investment club meetings, with institutional clients and by corporate finance and underwriting department personnel. The film will also serve as an excellent audio-visual training aid for new registered representatives.

Enclosed is an informational flier describing the motion picture with a convenient order form attached for your use in borrowing a print. If you wish to purchase a film print outright for firm use, the price, including shipping carton, reel and can, is $75.00 a copy and your check should accompany your order to the Information Department, National Association of Securities Dealers, Inc., 1735 K Street, N. W., Washington, D. C. 20006.

Sincerely,

John H. Hodges, Jr.

John H. Hodges, Jr.
Senior Vice President
Member Services

Enclosure

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

October 17, 1972

To: All NASD Members

Re: Missing Certificates of Northeast Petroleum Industries, Inc.

The NASD has recently been notified that blank unissued stock certificates of Northeast Petroleum Industries, Inc. have been lost during shipment. These certificates are for Boston Registry and bear the numbers C8879 through C9000. When lost, the certificates did not bear a valid signature of the Transfer Agent or the Registrar.

If an NASD member comes into the possession of any of the certificates bearing one of the above listed numbers, or any questionable certificate, he should contact: Mr. Nicholas A. Saporito, Vice President, Stock Transfer Division, First National Bank of Boston, P. O. Box 644, Boston, Massachusetts 02102 (617) 434-6544.

Sincerely,

John S. R. Schoenfeld

John S. R. Schoenfeld
Executive Vice President

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

October 17, 1972

ATTENTION OPERATIONS OFFICERS

To: All NASD Members

Re: Equitable Equities, Inc.; Havener Securities Corp.; and C. I. Oren & Co., Inc.

The NASD's Uniform Practice Committee has been advised that a SIPC Trustee has been appointed for Equitable Equities, Inc., of New York City, and temporary receivers have been appointed for Havener Securities Corp. and C. I. Oren & Co., Inc., both of New York City. The Committee has determined that members may use the immediate close-out procedures under Section 59(h) of the Uniform Practice Code for open transactions with the above named firms.

Please refer to Section 59(h) of the Code for the detailed procedures.

All money differences and other matters of business should be taken up with the below named individuals:

For: Equitable Equities, Inc.
233 Broadway
New York, New York 10007
Telephone: (212) 349-0400

Trustee: Herbert S. Camitta, Esq.
(can be reached through the firm)

For: Havener Securities Corp.
111 Broadway
New York, New York 10006
Telephone: (212) 964-2555

Receiver: Ezra G. Levin, Esq.
(can be reached through the firm)

For: C. I. Oren & Co., Inc.
39 Broadway - Room 2501
New York, New York 10006
Telephone: (212) 425-5593

Receiver: Martin R. Gold, Esq.
(can be reached through the firm)

-continued-

Questions regarding this notice should be directed to the Member Operations Department, 2 Broadway, New York, New York 10004 (212) 269-6393.

Sincerely,

John S. R. Schoenfeld

John S. R. Schoenfeld
Executive Vice President

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

October 23, 1972

To: All NASD Members

Re: Missing Municipal Bonds

The NASD has recently been notified that the following municipal bonds have been either lost or stolen:

$10,000	Arizona Board of Regents Educational Facility Revenue Series A for the University of Arizona, dated 9-1-66, 5%, and due 6-1-91. Bond Nos. A1831 and A1832
$10,000	Same as above, 5%, due 6-1-86 Bond Nos. A1208 and A1209
$50,000	Mohave Union High School District, Mohave County, Arizona Series of 1968, dated 6-1-68, 4.6%, and due 6-1-84. Bond Nos. 287 through 296
$15,000	Northern Cochise County Hospital District, Cochise County, Arizona Series of 1966, dated 6-30-66, 4.75%, and due 6-30-79. Bond Nos. 24, 25 and 26
$15,000	Same as above, 4.75%, due 6-30-80. Bond Nos. 27, 28 and 29
$50,000	Pima County School District No. 13 (Tanque Verde) of Pima County, Arizona Project of 1970, dated 7-1-70, 7%, due 6-1-85. Bond Nos. 72 through 81
$25,000	Phoenix Public Housing Authority, Phoenix, Arizona Series of 1951, 2 1/8 %, due 8-1-83 Bond Nos. 2826 through 2850
$20,000	San Pedro Valley Hospital District, Cochise County, Arizona Series of 1968, dated 10-1-68, 5%, due 6-30-76 Bond Nos. 16 through 19

-continued-

$25,000	San Pedro Valley Hospital District, Cochise County, Arizona Series of 1968, dated 10-1-68, 5%, due 6-30-77. Bond Nos. 20 through 24
$10,000	Same as above, 5%, due 6-30-78 Bond Nos. 25 and 26
$50,000	Tucson Water Revenue, Tucson, Arizona Series of 1965, dated 6-1-65, 3.4%, due 6-1-91 Bond Nos. 823 through 832

All of the missing securities are bearer bonds.

If an NASD member comes into the possession of any of the bonds bearing one of the above listed numbers, or any questionable bond, he should contact: Barry Peacock, Young, Smith & Peacock, 3443 North Central Avenue, Suite 100, Phoenix, Arizona 85012 (602) 264-9241.

Sincerely,

John S. R. Schoenfeld

John S. R. Schoenfeld
Executive Vice President

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

October 23, 1972

To: All NASD Members (Attention Operational Officers)

Re: Bovers, Parnass & Turel , Inc.
One Exchange Place - Room 914
Jersey City, New Jersey 07302
(212) 285-9037

Albert & Maguire Securities Co., Inc.
2383 D Cottman Avenue
Roosevelt Mall
Philadelphia, Pennsylvania 19149
(215) 331-8220

The NASD's Uniform Practice Committee has been advised that SIPC Trustees have been appointed for the above-mentioned firms. Pursuant to this the Committee has determined that members may use the immediate close-out procedure under Section 59(h) of the Uniform Practice Code for open transactions with these firms.

All money differences and other matters of business should be taken up with the below-named trustees:

For: Bovers, Parnass & Turel, Inc.

Trustee: Edward J. Rasner, Esq.
Chase, Leyner, Holland & Tarleton
549 Summit Ave.
Jersey City, New Jersey
(201) 656-2030

For: Albert & Maguire Securities Co., Inc.

Trustee: Donald M. Collins, Esq.
Waters, Fleer, Cooper & Gallager
Three Parkway - Suite 624
Philadelphia, Pennsylvania 19102
(215) LO-8-2517

Please refer to Section 59(h) of the Uniform Practice Code for the detailed procedures. Questions regarding this notice may be directed to the NASD, Inc., Member Operations Department, Two Broadway, New York, New York 10004 (212) 269-6393.

Sincerely,

John S. R. Schoenfeld

John S. R. Schoenfeld
Executive Vice President

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

October 27, 1972

TO: NASDAQ COMPANIES
NASD MEMBERS AND BRANCH OFFICES
NEWSPAPER FINANCIAL EDITORS

During the past several years, and especially since the start of the NASDAQ System in February 1971, the NASD has been actively committed to producing a fair and informative collection of over-the-counter quotations and volume information on an orderly basis through wider news media coverage. This effort has been made to keep pace with growing investor interest and increased activity in the OTC market. While we have made progress in expanding such coverage, we have found that we are faced with certain problems which are currently hampering our efforts with respect to expanding coverage in the national OTC quotation list of issues carried by many major newspapers across the country.

The NASDAQ Committee, charged by the Association's Board of Governors with the responsibility for supervision over collection of such quotes, therefore desires to apprise NASD members and registered representatives, NASDAQ issuers, newspapers and other interested parties of the current situation and with this letter is also soliciting ideas and assistance to improve OTC quotations coverage in newspapers.

Under the present system of newspaper quotations, there is a National List of over-the-counter issues and local lists under the immediate supervision of local quotations committees. The National List is, in general, transmitted throughout the country by the newswire services for publication in major newspapers. The local quotations list mentioned above comprised of OTC issues selected by the local NASD Quotations Committees are selected on the basis of regional investor interest and issues quoted therein meet certain minimum standards as set forth by the Association's Board of Governors. The National List is composed of 1,650 issues drawn from the approximately 3,450 issues currently quoted in the NASDAQ System while local lists include both issues quoted in NASDAQ as well as those with purely regional appeal.

Historically, a major part of the criteria for selecting issues which newspapers quote has been the number of shareholders of an issue within the general circulation area of the publication. A shareholder is viewed as a potential buyer of a newspaper and this has been the key to the reader interest factor so important to financial editors.

However, as the OTC market has grown over the years, newspapers have not been able to furnish the additional space needed to carry quotations on all of the issues which the NASDAQ Committee believes, because of interest and trading activity, deserve quotations coverage.

Our experience with the National List illustrates this problem. Fifteen years ago, a company could qualify for the National List with as few as 600 shareholders. However, over the years as the number of issues increased, the number of shares and stockholders also grew. Also, additional space in newspapers became difficult to obtain. The minimum shareholder requirement was increased. Today an issue must have 1,500 shareholders with a minimum distribution of 300 shareholders in two of four regional divisions or in the alternative a minimum of 2,000 shareholders throughout the nation. To compound the problem further, some companies which achieved early entry into the National List have not retained the initial activity and investor interest which qualified them for the list. Thus, their continued inclusion might, with space at a premium, no longer be fully justifiable.

Consequently, the NASDAQ Committee has been studying alternative steps which it might take to restructure this list to sharpen reader interest so that newspapers will be encouraged to improve and expand their quotations coverage of the OTC market.

One alternative is to continue the basic approach currently in use of basing National List selections on shareholder data and other criteria. Our recent experience, however, indicates that obtaining current, accurate stockholder data is growing more difficult. A large and growing percentage of stock outstanding is held in "street name" and companies are unable to provide us with accurate stockholder data without making inquiries to broker/dealers for detailed breakdown of shares which are registered in the names of broker/dealers. For example, in the last solicitation from the NASDAQ Committee for such data from companies quoted in NASDAQ, a substantial number of companies failed to respond.

Another alternative under study is to select issues for the National List based primarily upon trading volume. It would be possible to compose the National List of the most actively traded securities in the NASDAQ System. This approach is likely to cause a substantial revision in the composition of the present list. It does offer the possibility, however, that newspapers will view such a list as representing the highest degree of reader interest.

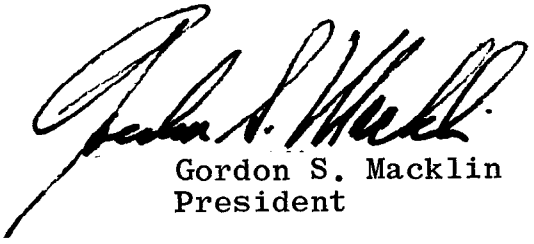
Notwithstanding any change which may finally be adopted by the Association, the NASDAQ System will continue to release to the newswire services the quotations and volume on substantially all of the 3,450 issues in the System so that newspapers will continue to have access to this information on any issues in which they have particular interest. Also, as to any issue which will be removed and replaced because of revised criteria, every effort will be made to have NASD local quotations committees add to their respective local lists those securities which might be deleted from the National List as new standards are adopted to improve the newspaper coverage of the OTC market. Thus, the authority of the local committees to select which issues they desire quoted in their regions is expected to continue.

Currently, the FINANCIAL WEEKLY, published by Media General, presents weekly data on quotations and volume for the complete list of NASDAQ securities that are released to the newswire services. We will, of course, continue to make every effort to have daily newspapers expand their coverage of the over-the-counter market and to interest other financial publications in introducing the full NASDAQ list showing quotations and volume on a daily basis.

With these considerations set forth and keeping in mind our goals, the Association is most interested in having the benefit of the comments of your organization as to what might be done to increase newspaper quotation coverage so that the publication of such quotes will be fair and informative and provide the greatest amount of information on over-the-counter issues to the public.

We would appreciate receiving any such comments by November 17, 1972. Please direct your comments to the NASDAQ Department, National Association of Securities Dealers, Inc., 1735 K Street, N. W., Washington, D. C. 20006.

Sincerely,



Gordon S. Macklin
President

Carrillo

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

November 6, 1972

TO: All NASD Members and Interested Persons

RE: Proposed Amendments to Regulations Governing Sales Charges on Mutual Fund Shares and Variable Annuity Contracts

1. Proposed Amendments to Subsections (a) and (d) of Article III, Section 26 of Rules of Fair Practice

2. Proposed Amendment to Subsection (c) of Article III, Section 29 of Rules of Fair Practice

The Board of Governors of the Association has proposed amendments to existing regulations, as referenced above, which are being published at this time to enable all interested persons to comment thereon. Such comments must be in writing and received by the Association on or before December 6, 1972, in order to receive consideration. After the comment period has closed, the proposed amendments must again be reviewed by the Board taking into consideration the comments received. Thereafter, upon approval by the Board, they must be submitted to the membership for a vote. If approved, the proposals must be submitted to and not disapproved by the Securities and Exchange Commission prior to becoming effective.

The authority for these proposals is contained in Section 15A (b) (8) of the Securities Exchange Act of 1934, as amended (the Maloney Act), 15 USC 78o-3 (b) (8); Section 22 of the Investment Company Act of 1940, as amended, 15 USC 80a-22, and Article VII of the Association's By-Laws.

Background and Explanation of Proposals

Under the 1970 Amendments to Section 22 (b) of the Investment Company Act of 1940, the NASD has the obligation to formulate and enforce rules preventing sales charges on mutual fund shares which are "excessive". In establishing such rules, the allowance of "reasonable compensation for sales personnel, broker-dealers, and underwriters", and the imposition of "reasonable" sales charges for investors is specifically provided for in the legislation. To assist

in the objective formulation of sales charge rules, the Association engaged a firm of independent consultants to undertake an intensive "Economic Study of the Distribution of Mutual Funds and Variable Annuities" ("Study") with the objective of formulating criteria for the appraisal of sales charges in light of all relevant factors.

As originally understood, the Study was to have covered sales charges only for open-end investment company shares. However, at the request of the SEC, the scope of the Study was widened to include contractual plans and variable annuity contracts, as well as consideration of alternative methods of distributing mutual fund shares. All phases of the Study have now been completed. Without necessarily endorsing all aspects of the Study, the Association has, after review of the Study facts and conclusions, accepted the regulatory approach recommended by the consultants and the proposed amendments to Article III, Sections 26 and 29 of the Association's Rules of Fair Practice.

The guiding considerations that underlie the proposed rules are the protection of investors and the maintenance of an industry structure that will promote services of a high quality. To insure these objectives, the proposals are not the result of a particular formula, but reflect a judgmental weighing of factual evidence bearing on the following four standards used for evaluation of the reasonableness of the sales charges:

1. Effective competition: Competition may take the form of price and product competition. The Association is directing its regulatory authority, as a supplement to market forces, toward remedying imperfections in the market so as to assure a price-product structure consistent with effective competition. The objective is to maintain a sales charge structure where the sales charge declines as the size of the purchase increases and where higher sales charges are accompanied by better terms.

2. Value of Service: Charges to the investor must not exceed the value provided to the investor by diversification plus: (a) the value of various product features; and (b) the value of services rendered coincident with the sale of investment company securities. The value to the investor is measured by the cost that the investor would incur if he sought on his own to purchase the benefits and services he received through the acquisition of investment company securities.

3. Salesmen's Compensation: Sales charges must allow for compensation levels that are sufficient to attract personnel commensurate with the quality of the service required, giving consideration to the time spent in the selling effort, the level of education, and professional experience of sales personnel.

4. Cost of Distribution: Sales charges should be sufficient to cover the costs incurred by underwriters and broker-dealers plus

a reasonable allowance for profit. The relevant costs are those functionally related to the sales of investment company securities within an industry structure characterized by a sufficient number of efficiently managed large and small firms to insure effective competition.

The results of the application of these standards, both in terms of conclusions expressed in the Study and in terms of the relationship of these conclusions to the proposed amendments to the rules, are discussed separately as they relate to sales charges on mutual fund shares, variable annuity contracts, and contractual plans.

Sales Charges on Mutual Fund Shares -- Proposed Amendments to Section 26

Proposed Amendment to Subsection (a)

The proposed amendment to subsection (a) of Section 26 is a conforming amendment necessitated by those provisions contained in the proposed amendments to subsection (d) pertaining to "single payment" investment plans issued by a unit investment trust registered under the Investment Company Act of 1940.

Proposed Amendment to Subsection (d)

The proposed amendment to subsection (d) of Section 26 would prevent members from selling shares of an open-end investment company or a single payment investment plan issued by a unit investment trust registered under the Investment Company Act of 1940 if the public offering price includes a sales charge which is excessive taking into consideration all relevant circumstances. Following this general prohibition are several provisions which if not conformed to would deem a sales charge to be excessive. These provisions were developed taking into consideration the four regulatory criteria discussed above.

The application of the four regulatory criteria to the distribution of mutual fund shares reflects the following:

1. Effective Competition: During the decade of the 1960's, the competitive forces in the industry brought about significant improvements in the terms on which investors are able to acquire mutual funds. The Study clearly indicates that there has been a decline in the minimum purchases needed to benefit from quantity discounts; the availability of cumulative quantity discounts has become more widespread; an increasing proportion of funds offer reinvestment of dividends without sales charges; and exchange and combination privileges are now offered by virtually all underwriters selling several funds. These improvements in the terms, together with other factors, have resulted, despite a rise in maximum sales charges, in a 30 percent decline in the average sales charge to

investors, from 6.3 percent in 1960 to 4.4 percent in 1970. The investor has also benefited from lower minimum purchase requirements, a widespread offering of retirement plan services, and an improvement in the conditions of eligibility for withdrawal plans.

While the Study shows that the price-product structure is generally consistent with conditions of effective competition, the proposed amendments to subsection (d) of Section 26 are intended to improve competition in the following areas:

(a) The disparities in maximum sales charges among the various funds were not generally found to be product related; i.e., funds with a higher maximum sales charge do not generally offer better terms than funds with a lower maximum. Proposed subsection (d) (1) of Section 26 therefore prohibits sales charges which exceed an established maximum level under any circumstances.

(b) The Study revealed that a significant proportion of mutual funds offering reinvestment of dividends at regular sales charges do not have lower maximum sales charges or offer better terms than funds offering dividend reinvestment without sales charges (i.e., at net asset value). Consequently, proposed subsection (d) (2) of Section 26 provides that if reinvestment of dividends at net asset value is not offered, there shall be a stated reduction from the maximum sales charge otherwise authorized. If dividends are reinvested at net asset value, a reasonable service fee may be charged for each dividend reinvestment transaction.

(c) According to the Study, a significant proportion of mutual funds that do not offer cumulative quantity discounts to individuals do not have lower maximum sales charges or offer investors better terms than funds that do offer such discounts. Accordingly, proposed subsection (d) (3) of Section 26 provides that if cumulative quantity discounts are not offered, there shall be a stated reduction from the maximum sales charge otherwise authorized.

(d) The Study found considerable variance in the discounts granted for volume purchases. As a result, proposed subsection (d) (4) of Section 26 establishes minimum standards for quantity discounts for the first and second gradations, or breakpoints. If the quantity discounts offered do not meet these minimum standards, there shall be a stated reduction from the maximum sales charge otherwise authorized.

The reductions in maximum sales charge required by the above proposals are cumulative so that if, for example, none of the specific services offered meet the minimum requirements of the rule, the maximum permissible sales charge on any transaction would be 6 percent.

2. Value of Service: The Study supports the conclusion that the proposed rule amendments will result in a structure of sales charges where the value of service received by the investor exceeds the cost of acquisition, giving consideration to the diversification needed to reduce risk, the benefit of other product features, and the services rendered by salesmen. This is particularly true for the smaller investors.

3. Salesmen's Compensation: The Study shows that relatively few salesmen earn substantial incomes from the sales of mutual fund shares. It is pointed out as well that, in relation to the sales effort involved, the structure of sales charges does not permit or encourage "excessive" compensation to mutual fund salesmen.

4. Cost of Distribution: According to the Study, the existing structure of sales charges did not provide "excessive" compensation for underwriters or broker-dealers in recent years. Moreover, in 1970, the last year for which data are available, only the largest, diversified, broker-dealer firms achieved profitable operations from their mutual fund business.

The proposed rule amendments are in the form of alternatives and have been limited to the four most important variables that bear on the effective sales charge paid by investors: the maximum sales charge, quantity discounts, dividend reinvestment, and rights of accumulation. The proposals are intended to be sufficiently flexible to permit adjustments based on an assessment of changing competitive conditions in the particular market that is served and to allow innovations in product features, services, and distribution methods.

It is recognized that other aspects, such as exchange and combination privileges, and letters of intent, also influence the effective sales charges. The Association intends to keep these and other product features offered under surveillance and, if necessary, make such features the subject of specific rules. The surveillance is intended to guard against attempts to circumvent the effect of the proposed amendments by changing the terms on which product features are now offered to investors or by instituting charges or special fees for the redemption of outstanding mutual fund shares, or for other services or features not covered specifically in the proposed rule amendments.

Sales Charges on Variable Annuities -- Proposed Amendments to Section 29

In view of the fact that variable annuities differ substantially from mutual funds, particularly with respect to industry structure,

degree of maturity, regulatory aspects, and price-product characteristics, separate rules are required for variable annuity sales charges. Nevertheless, the same four criteria or standards of regulation are relevant to an appraisal of sales charges in order to protect the investor and assure the viability of the variable annuity industry. Important considerations, too, in formulating the rules are the "infant industry" status of the variable annuity business and the dual nature of the product (i.e., securities and insurance) resulting in a complex regulatory framework that involves the SEC, State Insurance Commissioners, and the NASD.

With respect to the four regulatory criteria adopted, some primary Study conclusions and their relationship to the proposed rules follow:

1. Effective Competition: Given the present degree of industry maturity, competition is generally developing satisfactorily with respect to rate of entry and on a price-product basis. Because of the "infant industry" status of the industry, the nature of developing competition rather than the status of existing competition, is the relevant yardstick. The Study concluded as well that the existing level of charges on variable annuities generally is not excessive either from the investor's or the industry's viewpoint.

However, the existence of certain market imperfections was disclosed by the Study, which the Association's proposed rules are intended to remedy:

(a) A wide diversion of prices and price structures currently exists in a market where higher sales charges may not always be accompanied by better terms. Consequently, proposed subsection (c) (1) of Section 29 provides that sales charges on variable annuity contracts shall not exceed an established percentage of purchase payments in the first twelve contract years.

(b) It was brought out in the Study that approximately three-fourths of single payment variable annuity contracts provide for graduated sales charges based on the size of purchase payments. Therefore, proposed subsection (c) (2) of Section 29 requires that a specific minimum scale of graduated sales charges be offered.

(c) In a very few contracts, deductions from purchase payments are not separated according to the nature of the expenses that they cover. Consequently, the Study concluded that in such cases it is not possible to determine what part of the charge is for sales and what part is for administrative expenses. Proposed subsection (c) (3) of Section 29 therefore requires that if the charges are not stated separately,

the total charge shall be regarded as a sales charge and brought within the established limitations.

(d) A further conclusion of the Study was that future competition may be enhanced through the establishment of more stringent disclosure requirements and lifting of the current "blanket" restrictions on hypothetical illustrations. The Association agrees with that conclusion; however, it is believed that these issues will require additional work and separate recommendations by the Association to the SEC.

2. Value of Service: It was concluded that the value of service provided to investors by variable annuities through portfolio diversification and dividend reinvestment alone, i.e., without consideration of any other product features, exceeds the sales charge for most plan purchasers. This conclusion is based on calculations using the average monthly purchase payment of approximately $100 under periodic payment variable annuity contracts. Moreover, variable annuities provide a "bundle" of product features, which cannot be assembled through alternative retirement-planning instruments at the present time.

3. Salesmen's Compensation: The Study concluded that compensation earned by full-time agents on sales of variable annuity contracts is not excessive when compared with compensation from available alternative sources.

4. Cost of Distribution: Because of the newness of variable annuity operations for most carriers, costs of these operations could not be considered in the Study as an appropriate standard for regulating sales charges. Current costs are not representative of future long-term costs and owing to the product mix of carriers there are limitations in distinguishing those costs arising from variable annuity operations. The Study makes clear from available cost data, however, that current sales charges fall far short of covering current distribution costs.

The conclusions reached in the Study, and the proposed amendments to Section 29 regarding sales charges on variable annuities, are largely influenced by the early stage of development of variable annuity operations. Consequently, they must be re-evaluated as regulatory experience is gained in this area and as the industry grows. However, the Association believes that the proposed rule will have a strengthening influence on competition in the course of future industry development.

Too, the proposed rule addresses only the maximum sales charge and the structure of sales charges. It has been formulated in light of the belief that the Association has no jurisdiction over charges made against purchase payments other than sales charges. Such other

charges would include those for administration and those for investment management and for the mortality and expense risks assumed by the insurance company, that are generally made against the assets of the separate account. The Association understands that the SEC has already assumed surveillance over charges for administration and in most instances requires issuers of variable annuities to disclose in their prospectuses that charges for administration will not exceed the cost of providing administrative services.

Contractual Plans

One of the principal areas of regulation changed by the 1970 Amendments to the Investment Company Act was the regulation of periodic payment contractual plans, particularly the levels of first year sales charge deductions on such plans.

Specifically, amended Section 27 of the Act provides a contractual plan sponsor with the choice of offering the conventional periodic payment contractual plan with up to 50 percent of the sales charge deducted from the first year's payments, but only if coupled with a refund offer to the planholder of his entire sales charge plus the underlying net asset value of the related mutual fund shares if requested 45 days from the start of the plan (this provision being commonly referred to as the 45-day "free look" privilege), and the right to receive a refund within 18 months after the start of the plan representing any excess paid for sales charges over 15 percent of the payments made by the planholder to that date plus the net asset value of his shares. Alternatively, the sponsor may offer a spread-load plan, pursuant to which not more than 20 percent of any payment may be deducted for sales charges from any of the first 36 monthly payments and not more than an average of 16 percent may be deducted from the first 48 monthly payments. Under this spread-load alternative, the sponsor is also required to offer the 45-day free look privilege.

As authorized by Section 27, the Commission also prescribed forms of notice to be furnished with the refund offers and substantial reserve requirements for plan sponsor companies with respect to the refund obligations. These new provisions were added to provisions in the original 1940 Act which, among other matters, fixed a 9 percent maximum sales charge on the total payments to be made and provided that not more than one-half of the first twelve monthly payments, or their equivalent, could be deducted for sales charges.

The Study clearly demonstrates that the amendments to Section 27 have contributed to major changes in the structure of the contractual plan industry, as described in the Study. As recently as early 1970, there were approximately 50 contractual plan sponsors offering 77 separate periodic payment contractual plans; at the beginning of 1972, only 30 sponsors were offering 49 separate plans. Prior to the 1970 Amendments, only one sponsor offered periodic payment contractual

plans on a spread-load basis; at the beginning of 1972, 21 of the 49 contractual plans still being offered were available on a spread-load basis. However, due to the limited amount of time that had elapsed since passage of the 1970 Amendments, the Study could not reflect either comprehensive data relating to the distribution of new contractual plan sales as between front-end and spread-load plans, or comprehensive data relating to the cost impact on plan sponsors associated with compliance with the provisions of amended Section 27. Moreover, since compensation arrangements of many plan sponsors and broker-dealers were still in a state of flux, it was impossible to assemble meaningful data with respect to the changes which have taken place in modes of compensation to sales personnel and broker-dealers on new plan sales as a result of the Amendments, and the consequences of such changes in sales incentives.

One of the most significant factors contributing to these changes, as recognized by the Study, is the 18 month refund provision. The first 18 months after the effectiveness of the Act will not have passed until December 14, 1972, and it will only be sometime thereafter, when analyses can be made of the significance of refunds during successive 18 month periods, changes in levels of compensation, and changes in the level and distribution of new sales between front-end load and spread-load plans, that the impact of the refund provision on the viability of the plan industry can be measured.

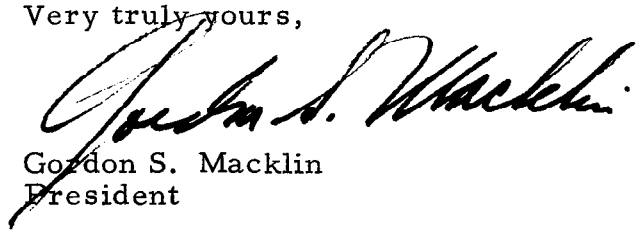
In these circumstances, and in view of the protection afforded to planholders by amended Section 27 of the Act, the Board has decided to defer the formulation of rules with respect to sales charges on periodic payment contractual plans until sufficient time has elapsed to permit an assessment of the impact of the amendments on the contractual plan industry and a determination of whether the level and structure of sales charges meet the standards specified by Section 22 (b) of the Act. While the proposed rules do not therefore apply to periodic payment plans, the Association will be monitoring further developments in the industry and rules may be necessary at some future time.

With respect to single payment contractual plans, the application of the four standards or criteria of regulation (i.e., effective competition, value of service, salesmen's compensation, and cost of distribution) led to conclusions similar to those drawn from the Study with respect to open-end investment company shares. Since these plans were essentially unaffected by the 1970 Amendments, the proposed amendments to Section 26 would apply to single payment contractual plans as well as regular purchases of mutual fund shares.

Comments on the proposed rules should be addressed to Mr. Donald H. Burns, Secretary, National Association of Securities

Dealers, Inc., 1735 K Street, N. W., Washington, D. C. 20006, on or before December 6, 1972. All communications will be considered available for inspection.

Very truly yours,



Gordon S. Macklin
President

Text of Proposals

Proposed Amendment to Article III, Section 26 of Rules of Fair Practice

New material indicated by underlining
Deleted material indicated by striking out

Subsection (a) of Section 26 is proposed to be amended as follows:

(a) Except for the provisions of subsection (d), this rule shall apply exclusively to the activities of members in connection with the securities of an "open-end management investment company" as defined in the Investment Company Act of 1940.

Subsection (d) of Section 26 is proposed to be amended as follows:

~~Gross Selling Commission~~ Sales Charge

(d) No member ~~who is an underwriter~~ shall ~~participate in the offering~~ or ~~in the sale~~ sell ~~of any such security~~ the shares of any open-end investment company or any "single payment" investment plan issued by a unit investment trust registered under the Investment Company Act of 1940 if the public offering price includes a ~~gross selling commission or load (i.e., the difference between the public offering price and the price received by the issuer)~~ sales charge which is ~~unfair~~ excessive, taking into consideration all relevant circumstances. ~~including the current marketability of such security and all expenses involved~~ Sales charges shall be deemed excessive if they do not conform to the following provisions:

(1) The maximum sales charge on any transaction shall not exceed 8.50% of the offering price.

(2) (a) Dividend reinvestment shall be made available at net asset value per share to "any person" who requests such reinvestment within 20 days prior to payment date, subject only to the right to limit the availability of dividend reinvestment to holders of securities of a stated minimum value, not greater than $1,200, and provided that a reasonable service charge may be applied against each reinvestment of dividends.

(b) If dividend reinvestment is not made available on terms at least as favorable as those specified in

subsection (2) (a), the maximum sales charge on any transaction shall not exceed 7.25% of offering price.

(3) (a) Rights of Accumulation (cumulative quantity discounts) shall be made available to "any person" for a period of not less than ten (10) years from the date of first purchase in accordance with one of the alternative quantity discount schedules provided in subsection (4) (a) below, as in effect on the date the right is exercised.

(b) If Rights of Accumulation are not made available on terms at least as favorable as those specified in subsection (3) (a), the maximum sales charge on any transaction shall not exceed:

(1) 8.0% of offering price if the provisions of subsection (2) (a) are met; or

(2) 6.75% of offering price if the provisions of subsection (2) (a) are not met.

(4) (a) Quantity discounts shall be made available on single purchases by "any person" in accordance with one of the following two alternatives:

(1) A maximum sales charge of 7.75% on purchases of $10,000 or more and a maximum sales charge of 6.25% on purchases of $25,000 or more; or

(2) A maximum sales charge of 7.50% on purchases of $15,000 or more and a maximum sales charge of 6.25% on purchases of $25,000 or more.

(b) If quantity discounts are not made available on terms at least as favorable as those specified in subsection (4) (a), the maximum sales charge on any transaction shall not exceed:

(1) 7.75% of offering price if the provisions of subsections (2) (a) and (3) (a) are met;

(2) 7.25% of offering price if the provisions of subsection (2) (a) are met but the provisions of subsection (3) (a) are not met;

(3) 6.50% of offering price if the provisions of subsection (3) (a) are met but the provisions of subsection (2) (a) are not met;

(4) 6.00% of offering price if the provisions of subsections (2) (a) and (3) (a) are not met.

(5) The term "any person" as used in this rule shall mean "any person" as defined in Rule 22d-1 (a) under the Investment Company Act of 1940.

Proposed Amendment to Article III, Section 29 of Rules of Fair Practice

New material indicated by underlining
Deleted material indicated by striking out

Subsection (c) of Section 29 is proposed to be amended as follows:

Sales ~~Load~~ Charges

(c) No member shall participate in the offering or in the sale of variable annuity contracts if the purchase payment includes a sales ~~load~~ charge which is ~~unfair~~ excessive: ~~taking into consideration all relevant circumstances.~~

(1) In contracts providing for multiple payments a sales charge shall not be deemed to be excessive if the contract provides for a sales charge which will not exceed 8.5% of the total payments to be made thereon as of a date not later than the end of the twelfth year of such payments, provided that if a contract be issued for any stipulated shorter payment period, the sales charge under such contract shall not exceed 8.5% of the total payments thereunder for such period.

(2) In contracts providing for single payments a sales charge shall not be deemed to be excessive if the contract provides for a scale of reducing sales charges related to the amount of the purchase payment which is not greater than the following schedule:

First $25,000 - 8.5% of purchase payment
Next $25,000 - 7.5%
Over $50,000 - 6.5%

(3) In contracts where sales charges and other deductions from purchase payments are not stated separately, the total deductions from purchase payments (excluding those for insurance premiums

and premium taxes) shall be treated as a sales charge for purposes of this rule and shall not be deemed to be excessive if they do not exceed the percentages for multiple and single payment contracts described in paragraphs (1) and (2) above.

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

November 9, 1972

ERRATA

TO: All NASD Members and Interested Persons

RE: Release Concerning Proposed Amendments to Regulations Governing Sales Charges on Mutual Fund Shares and Variable Annuity Contracts Dated November 6, 1972

1. Proposed Amendments to Subsections (a) and (d) of Article III, Section 26 of Rules of Fair Practice

2. Proposed Amendment to Subsection (c) of Article III, Section 29 of Rules of Fair Practice

The release dated November 6, 1972 concerning the Association's proposed sales charge rules for mutual fund shares and variable annuities inadvertently deleted certain language which was intended to be included as follows:

On Page 2, first full paragraph, last line: Delete the period after "Practice" and add "are based on this approach."

On Page 13, paragraph (c), third line: Add the following after the word "change": "as ~~defined in Section 2 (a) (34) of the Investment Company Act of 1940~~".

The referred to release should be considered to be amended as indicated.

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

November 17, 1972

PLEASE INSURE DISSEMINATION TO ALL

REGISTERED REPRESENTATIVES AND PRINCIPALS

TO: ALL NASD MEMBERS

RE: Securities Transactions by Registered Representatives, Principals, Employees and Associated Persons

The Association's National Business Conduct Committee has apprised the Board of Governors of an increasing number of disciplinary actions in which registered representatives, principals, employees, and associated persons have been involved in personal transactions in high-risk speculative ventures and unregistered issues. In many instances, such transactions have been effected without the consent or knowledge of the member.

This type of activity may expose both the participants and the member to potential violations of industry rules and regulations and, where the public is a party to such transactions, to the possibility of civil litigation. Severe sanctions have been imposed on registered personnel for failing to disclose transactions effected outside the scope of their regular employment and, on members, for failing to adequately supervise registered and unregistered personnel.

Accordingly, the Board wishes to remind the membership and registered personnel of their obligations and responsibilities in this area. Your attention is particularly directed to the following Rules of Fair Practice:

Section 1 - Paragraph 2151.02 - NASD Manual (new issue filing requirements)

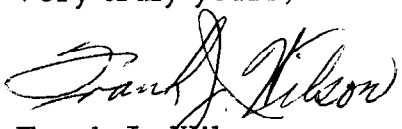
Section 2 - Paragraph 2152 - NASD Manual (subparagraph 4(e) on Page 2052 regarding private transactions)

Section 21(a) - Paragraph 2171 - NASD Manual (record-keeping requirements)

Section 27 - Paragraph 2177 - NASD Manual (supervisory responsibilities)

Section 28 - Paragraph 2178 - NASD Manual (transactions effected for personnel of other members)

Very truly yours,



Frank J. Wilson
Senior Vice President
Regulation

FJW/jm

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

November 17, 1972

To: All NASD Members

Re: Missing Certificates of Vagabond Motor Hotel, Inc.

The NASD has recently been notified that stock certificates of the Vagabond Motor Hotels, Inc. were reported stolen in a burglary of the Vagabond Motor Hotel, San Diego, California, on September 14, 1972. These certificates are described as non-negotiable and are issued in the name of Ronald A. Young. Description of the stolen certificates follows:

Certificate Number U24, 50,000 shares, issued July 31, 1968

Certificate Number U106, 1,000 shares, issued July 31, 1968

Certificate Number U107, 1,000 shares, issued February 15, 1972

Certificate Number DV481, 3,100 shares, issue date not known

If an NASD member comes into the possession of any of the above listed certificates, or receives any information concerning these certificates, he should notify the nearest office of the Federal Bureau of Investigation.

Sincerely,

John S. R Schoenfeld

John S. R. Schoenfeld
Executive Vice President

Barrillo

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

MAIL VOTE

IMPORTANT!

OFFICERS * PARTNERS * PROPRIETORS

To: Members of the National Association of Securities Dealers, Inc.

Date: November 29, 1972

Re: Mail Vote Concerning Proposed Amendment of Article III, Section 26 of Rules of Fair Practice to Add New Subsection (k) Re Execution of Investment Company Portfolio Transactions by Members Who Sell Investment Company Shares

LAST VOTING DATE IS December 29, 1972.

Enclosed herewith is a proposed amendment to Article III, Section 26 of the Association's Rules of Fair Practice which, pursuant to the provisions of Article IX of the Association's By-Laws, must be approved by the membership before it can become effective. The authority for the proposal is contained in Section 15A (b) (8) of the Securities Exchange Act of 1934, as amended (the Maloney Act), 15 USC 78o-3 (b) (8); Section 22 of the Investment Company Act of 1940, as amended, 15 USC 80a-22; and Article VII of the Association's By-Laws.

A proposed new subsection (k) to Article III of Section 26 (hereinafter called "Rule") was submitted to members and interested persons for comment on July 27, 1972. A significant number of helpful comments were received and, after careful consideration of these comments, changes in the proposed Rule were made by the Board of Governors.

Many of the comments received reflected concern with the provisions of paragraph (5) of the proposed subsection (k), which would have required members to "adopt procedures to insure that sales of investment company shares are not a factor in the selection of broker-dealers for execution of investment company portfolio transactions." The major concerns expressed were that this provision involved a subjective standard with which compliance would

have been difficult unless there was an avoidance of the execution of portfolio transactions for an investment company by members who sold shares of such investment company; that members would therefore be forced to choose between selling shares of an investment company and executing portfolio transactions for it; and that many members, particularly small firms located outside of the major financial centers, would be deprived of the opportunity of executing portfolio transactions for investment companies even though the first portion of the proposed paragraph (5) stated that nothing in the Rule "shall be deemed to prohibit the execution of investment company portfolio transactions by members who also sell shares of the investment company."

In light of these comments, the Board has revised paragraph (5) to clarify its intent, by stating that there is no prohibition against the execution of investment company portfolio transactions by members who also sell shares of the investment company provided members "seek orders for execution on the basis of the value and quality of their brokerage services and not on the basis of their sales of investment company shares." The earlier provision requiring members to adopt procedures to insure that sales of investment company shares are not a factor in the selection of broker-dealers for the execution of investment company portfolio transactions has been deleted.

No other material changes have been made in the text of the proposed Rule or Interpretation as previously submitted to the membership.

Background and Explanation of Proposal

The proposed Rule is intended to prohibit members from favoring or disfavoring the distribution of particular investment companies on the basis of brokerage commissions, soliciting or making promises of an amount or percentage of brokerage commissions in connection with the distribution of investment company shares, and seeking orders for the execution of portfolio transactions on the basis of their sales of investment company shares. The proposed Interpretation, which is designed to make clear the intent of the Rule, is included herewith for the information of members although a membership vote is not required.

In its Statement on the Future Structure of the Securities Markets in February, 1972, the Securities and Exchange Commission stated that it was requesting the NASD to direct its members to discontinue the use of reciprocal portfolio brokerage for the sale of investment company shares. In a letter to the Association, the Commission's Chairman, on behalf of the full Commission, reiterated the conclusions of the Statement on Future Structure concerning the potential regulatory problems deemed to be created by this practice. The Commission's Chairman has subsequently said that after the NASD moves to adopt its Rule, the Commission expects to publish a companion SECO rule to assure equality of treatment among all brokers and to look at the extent to which others,

not affected by NASD rules, engage in similar reciprocal practices.

The Association's Board of Governors accepts as a fact that it is customary for most investment companies whose shares are distributed by members of the Association to follow the policy publicly stated in their prospectuses of selecting for the execution of portfolio transactions brokers who are in a position to provide the best execution. It recognizes also that the selection of brokers among those equally qualified to provide the best execution frequently has been made on the basis of sales of shares of the investment company.

During the development of the proposed Rule, the Association has reviewed various alternatives for the implementation of the Commission's request. The Association has determined that it is not in the public interest, nor in the best interests of investment company shareholders, to prohibit or to in any way inhibit, the execution of portfolio transactions by members who also sell shares of the investment company. The Association believes that an investment company should be permitted to select broker-dealers who may have sold its shares, so long as the selection is made on the basis of a broker's professional capability and not the volume of shares sold. Sales of investment company shares should not be a qualifying or disqualifying factor in the selection of a broker-dealer to execute portfolio transactions.

Section by Section Analysis

Paragraph (1) of the proposed Rule provides that no member shall directly or indirectly favor or disfavor the distribution of shares of any investment company or group of investment companies on the basis of brokerage commissions received or expected by such members from any source. "Any source" includes any investment company or group of investment companies and any "covered account". The term "covered account" is defined in paragraph (6) as meaning (a) any other investment company or account managed by the investment adviser of such investment company, or (b) any other account from which brokerage commissions are received or expected as a result of the request or direction of any principal underwriter of such investment company or of any affiliated person of such investment company or of such principal underwriter, or of any affiliated person of an affiliated person of such investment company. Some of the activities which would be prohibited by paragraph (1), and which are delineated in the proposed Interpretation of subsection (k), are as follows:

1. Providing to salesmen, branch managers, or other sales personnel any incentive or additional compensation for sales of shares of specific investment companies based upon the amount of brokerage commissions received or expected from any source. This prohibition includes bonuses, preferred compensation lists, sales incentive campaigns or contests, or any other method of compensa-

tion which provides an incentive to sales personnel to favor or disfavor any investment companies based upon brokerage commissions. (See subsection (a) (1) of Interpretation.)

2. Recommending specific investment companies to sales personnel or establishing "recommended", "selected", or "preferred" lists of investment companies, regardless of the existence of any special compensation or incentives to favor or disfavor the shares of such companies in sales efforts, if such companies are recommended or selected on the basis of brokerage commissions received or expected from any source. (See subsection (a) (2) of Interpretation.)

3. Granting to salesmen, branch managers, or other sales personnel any participation in brokerage commissions received by such member from portfolio transactions of an investment company whose shares are sold by such member, or from any covered account, if such commissions are directed by or identified with such investment company or covered account. (See subsection (a) (3) of Interpretation.)

Paragraph (1) of the proposed Rule would permit a member to compensate its salesmen and branch managers based upon total sales of investment company shares attributable to such persons, whether by use of overrides, accounting credits, or other compensation methods if such compensation is not designed to favor or disfavor sales of shares of investment companies on a basis prohibited by the proposed new subsection. (See subsection (a) (5) of Interpretation.)

Paragraph (2) of the proposed Rule would prohibit any member from, directly or indirectly, demanding, requiring, or soliciting an offer or promise of an amount or percentage of brokerage commissions from any source in connection with or as a condition to the sale of shares of an investment company. This paragraph would not only prohibit a member from making the receipt of brokerage commissions a condition to the distribution of shares of an investment company but would prohibit a member from using sales of investment company shares as a factor in negotiating the price of, or the amount of brokerage commissions to be paid on, a portfolio transaction of an investment company or covered account, whether such transaction is executed in the over-the-counter market or elsewhere. (See subsection (a) (4) of Interpretation.)

Paragraph (3) of the proposed Rule would prohibit a member from, directly or indirectly, offering or promising to another member, or requesting or arranging for the direction to any member, of an amount or percentage of brokerage commissions from any source as an inducement or reward for the sale of shares of an investment company. This paragraph would, among other things,

prohibit an underwriter member from suggesting, encouraging, or sponsoring any incentive campaign or special sales effort for another member with respect to the shares of any investment company which incentive or sales effort is, to the knowledge or understanding of such underwriter member, to be based upon, or financed by, brokerage commissions directed or arranged by the underwriter member. (See section (b) of Interpretation.)

Paragraph (4) of the proposed Rule would prohibit members from circulating any information regarding the amount or level of brokerage commissions received by the member from an investment company or covered account to anyone other than management personnel who are required, in the overall management of the member's business, to have access to such information.

Paragraph (5) of the proposed Rule states that nothing in subsection (k) shall be deemed to prohibit the execution of portfolio transactions of investment companies by members who also sell shares of the investment company. It permits members who sell shares of an investment company to execute portfolio transactions for that investment company and its covered accounts so long as they seek to obtain such orders for execution on the basis of the value and quality of their brokerage services and not on the basis of their sales of investment company shares.

Paragraph (5) of the proposed Rule means that sales of investment company shares shall not be a qualifying or disqualifying factor in the selection of a broker-dealer to execute portfolio transactions. That choice must be made strictly on the basis of a broker-dealer's professional capability. This paragraph makes clear that a violation of the Rule could not be proven merely by demonstrating that a member has sold shares of an investment company for which it has executed transactions. Any investment company would be justified in placing orders for portfolio transactions -- and any member in executing them -- on the basis of the value and quality of the brokerage services rendered.

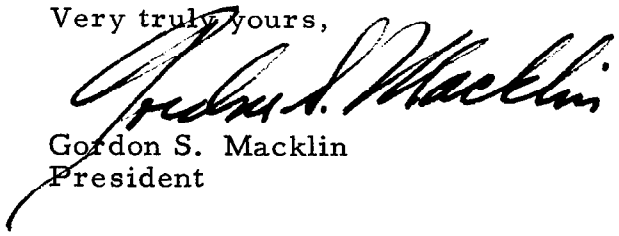
Paragraph (6) of the proposed Rule consists of two definitions. The first (the definition of "covered account") is discussed above in connection with paragraph (1) of the proposed Rule. The term "brokerage commissions", as defined in paragraph (6) of the proposed Rule, is not limited to commissions on agency transactions but also includes underwriting discounts or concessions and fees paid to members in connection with tender offers.

This proposed Rule, consisting of an amendment to Section 26 of Article III of the Rules of Fair Practice, is important and merits your immediate attention. Please mark your ballot according to your convictions and return it in the enclosed stamped envelope to "The Corporation Trust Company". Ballots must be postmarked no later

than December 29, 1972.

The Board of Governors believes this amendment is necessary and appropriate and recommends that members vote their approval.

Very truly yours,



Gordon S. Macklin
President

Proposed New Subsection (k) to Article III, Section 26 of the Rules of Fair Practice

Execution of Investment Company Portfolio Transactions

(k) (1) No member shall, directly or indirectly, favor or disfavor the distribution of shares of any investment company or group of investment companies on the basis of brokerage commissions received or expected by such member from any source, including such investment company, or any covered account.

(2) No member shall, directly or indirectly, demand, require, or solicit an offer or promise of an amount or percentage of brokerage commissions from any source in connection with, or as a condition to, the sale of shares of an investment company.

(3) No member shall, directly or indirectly, offer or promise to another member, or request or arrange for the direction to any member, of an amount or percentage of brokerage commissions from any source as an inducement or reward for the sale of shares of an investment company.

(4) No member shall circulate any information regarding the amount or level of brokerage commissions received by the member from any investment company or covered account to other than management personnel who are required, in the overall management of the member's business, to have access to such information.

(5) Nothing herein shall be deemed to prohibit the execution of portfolio transactions of any investment company or covered account by members who also sell shares of the investment company; provided, however, that members shall seek orders for execution on the basis of the value and quality of their brokerage services and not on the basis of their sales of investment company shares.

(6) Definitions

a. Covered Account shall mean (i) any other investment company or other account managed by the investment adviser of such investment company, or (ii) any other account from which brokerage commissions are received or expected as a result of the request or direction of any principal underwriter of such investment company or of any affiliated person (as defined

in the Investment Company Act of 1940) of such investment company or of such principal underwriter, or of any affiliated person of an affiliated person of such investment company.

b. Brokerage Commissions as used herein, or in any Interpretation hereof by the Board of Governors, shall not be limited to commissions on agency transactions but shall include underwriting discounts or concessions and fees paid to members in connection with tender offers.

Proposed Interpretation of New Subsection (k)

Pursuant to the provisions of Article IV, Section 2 (b) and Article VII, Section 3 (a) of the By-Laws, the following Interpretation has been adopted by the Board of Governors:

It shall be deemed conduct inconsistent with just and equitable principles of trade and in violation of Article III, Sections 1 and 26 (k) of the Rules of Fair Practice, for any member, subsequent to the effective date of this Interpretation, to engage in any of the following activities:

(a) With respect to a member's retail sales of shares of investment companies:

(1) To provide to salesmen, branch managers or other sales personnel any incentive or additional compensation for the sale of shares of specific investment companies based on the amount of brokerage commissions received or expected from any source including such investment companies or any covered accounts (as defined in Section 26 (k) of Article III of the Rules of Fair Practice) of such investment companies. Included in this prohibition are bonuses, preferred compensation lists, sales incentive campaigns or contests, or any other method of compensation which provides an incentive to sales personnel to favor or disfavor any investment company or group of investment companies based on brokerage commissions.

(2) To recommend specific investment companies to sales personnel, or establish "recommended", "selected", or "preferred" lists of investment companies, regardless of the existence of any special compensation or incentives to favor or disfavor the shares of such company or companies in sales efforts, if such companies are recommended or selected on the basis of brokerage commissions received or expected from any source.

(3) To grant to salesmen, branch managers or other sales personnel any participation in brokerage commissions received by such member from portfolio transactions of an investment company whose shares are sold by such member, or from any covered account, if such commissions are directed by, or identified with, such investment company or any covered account.

(4) To use sales of shares of any investment company as a factor in negotiating the price of, or the amount of brokerage commissions to be paid on, a portfolio transaction of an investment company or of any covered account, whether such transaction is executed in the over-the-counter market or elsewhere.

(5) Nothing herein shall prevent a member from compensating its salesmen and managers based on total sales of investment company shares attributable to such salesmen or managers, whether by use of overrides, accounting credits, or other compensation methods, provided that such compensation is not designed to favor or disfavor sales of shares of particular investment companies on a basis prohibited by this Interpretation.

(b) With respect to a member's activities as an underwriter of investment company shares,to suggest, encourage, or sponsor any incentive campaign or special sales effort of another member with respect to the shares of any investment company which incentive or sales effort is, to the knowledge or understanding of such underwriter-member, to be based upon, or financed by, brokerage commissions directed or arranged by the underwriter-member.

Mr. Parrillo

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 4, 1972

PLEASE INSURE DISSEMINATION TO ALL

MUTUAL FUND SALES MANAGERS

TO: ALL NASD MEMBERS

RE: SEC Announcement of Hearings on Mutual Fund Distribution and the Potential Impact of the Repeal of Section 22 (d) of the Investment Company Act of 1940

In Investment Company Act Release No. 7475 dated November 3, 1972, the Securities and Exchange Commission announced that it would commence public hearings on mutual fund distribution and the potential impact of the repeal of Section 22 (d) of the Investment Company Act of 1940. While the hearings were originally scheduled to begin on December 11, 1972, the Commission has announced that the hearing date has been postponed until February 12, 1973. Persons who wish to participate must file a written statement with the Commission by February 2, 1973.

According to the Commission's Release, the hearings will cover a broad range of subjects related to the distribution and sale of mutual fund shares, including, among other things, the effects of a complete or partial repeal of Section 22 (d) of the Investment Company Act (the retail price maintenance provision); the NASD's proposed Rules on mutual fund and variable annuity sales charges and the Study on which the Rules are based; various possible changes in sales charge structure; regulation of dealer discounts or commissions; and changes in current requirements regarding prospectuses, advertising, sales literature and group sales.

The issues to be discussed at the hearings are of major importance to the vast majority of NASD members involved in the sale of mutual fund shares and variable annuities. Members are urged to consider the issues outlined in the Commission's Release (copy attached) and the "Report of the Staff of the Securities and Exchange Commission On the Potential Impact of a Repeal of Section 22 (d) of the Investment Company Act of 1940" which has recently been published and to express their views on these issues to the Commission.

Very truly yours,

Frank J. Wilson

Frank J. Wilson
Senior Vice President
Regulation

FOR RELEASE November 3, 1972

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Investment Company Act of 1940
Release No. 7475
Securities Exchange Act of 1934
Release No. 9848

ANNOUNCEMENT OF HEARINGS ON MUTUAL FUND DISTRIBUTION AND THE POTENTIAL IMPACT OF THE REPEAL OF SECTION 22(d) OF THE INVESTMENT COMPANY ACT OF 1940

The Securities and Exchange Commission, having reviewed the Study of the Potential Economic Impact of the Repeal of Section 22(d) conducted by its Office of Policy Research and the Economic Study of the Distribution of Mutual Funds and Variable Annuities conducted for the National Association of Securities Dealers, Inc. ("NASD") by Booz Allen & Hamilton, Inc. has determined that it would be appropriate to re-examine traditional administrative positions and to explore new possibilities in order that mutual funds may be marketed more efficiently at a reasonable cost to investors. Section 22(d) requires, in part, that in the sale of a mutual fund security to the public the principal underwriter and any dealer must sell the security at a current public offering price -- net asset value plus stated sales charge - set forth in the prospectus.

In order to obtain a wide range of viewpoints with respect to the justification for this retail price maintenance provision in the distribution of mutual funds, as well as the options which would be open to the industry if Section 22(d) were eliminated and how the industry would adjust to such a change, the Commission has determined to commence public hearings on December 11, 1972.

Background

A. Study of the Potential Economic Impact of the Repeal of Section 22(d) of the Act.

In the Investment Company Amendments Act of 1970 (the "1970 Act") Congress took steps to improve the protection afforded mutual fund investors in the area of sales commissions. The Senate Committee on Banking, Housing and Urban Affairs indicated that "Partly because of Section 22(d) and partly because of the way in which mutual fund shares are sold, competition has tended to operate in reverse in the sale of mutual fund shares -- raising

prices rather than lowering them". 1/ The Committee gave serious consideration to deleting Section 22(d) from the Investment Company Act of 1940 (the"Act"). However, it was uncertain what that would mean to the investing public and mutual fund sales organizations. Therefore, it requested that the Commission review the consequences of such a proposal and report to it as soon as reasonably practicable.

Our staff is about to complete this study which will be released shortly. It deals among other things with the costs of distributing mutual funds, the earnings of those who sell mutual funds, the significance of revenue derived by brokerage firms from mutual fund sales and the significance of mutual fund sales to the securities markets. Before making any definitive recommendations to the Congress as to retail price maintenance the Commission believes it imperative to have the views of all interested persons with respect to the staff's report and the impact on the industry of various changes in the distribution system that may be desirable.

B. NASD Study and Rule Proposals

The 1970 Act gave the NASD rule-making authority to prevent mutual funds from being sold at a sales load which is "excessive". Under amended Section 22(b) of the Act mutual fund sales charges must allow for reasonable compensation for sales personnel, broker-dealers and underwriters, and reasonable sales loads to investors. The amendments also provide the Commission with the power to alter or supplement such NASD rules at any time after June 14, 1972 -- the effective date of this amendment. It was contemplated that during this period the NASD would study "all relevant factors" in order to provide a basis for its rule proposals. At the outset the Commission made clear that the NASD study should consider ways in which the existing distribution system could be improved with the resulting efficiencies and lower costs passed on directly to benefit investors and that the Commission would consider the feasibility of achieving this result in connection with its staff study of the impact of eliminating Section 22(d) from the Act.

1/ S. Rep. 91-184, 91st Cong. 1st Sess. 8 (May 21, 1969).

The NASD has now completed its study and has drafted rule proposals based upon it. That Study is, of course, a survey of mutual fund distribution as it has existed and the resulting rule proposals are premised on the continuation of that system and the existing regulatory framework. The authors of the Study indicated that "If Section 22(d) were repealed and sellers were able to set the prices of funds at levels other than their current offering price described in the prospectus, then the analysis presented . . . needs to be re-evaluated".

C. Other Developments

In our Statement on the Future Structure of the Securities Markets we announced that the practice of investment company managers using portfolio brokerage of mutual funds to reward broker-dealers for sales of fund shares must be terminated. The NASD has published for comment an amendment to Article III, Section 26 of its Rules of Fair Practice designed to implement this policy and is moving ahead expeditiously to adopt the necessary rule change.

The Commission recently liberalized the rules with respect to advertising of investment company securities. In the release announcing the changes we described them as a modest first step in this direction and requested further suggestions. 1/ Several have been received and are now under consideration.

It also is timely now to renew consideration of group merchandising of fund shares at reduced sales loads, long a controversial subject. Rule 22d-1 permits quantity discounts to be provided in connection with the sale of a mutual fund to any person but excludes from the definition of "person" any group whose funds are combined for such purchase. In 1968, the Commission proposed a revision of this anti-grouping provision. 2/ That proposal was held in abeyance pending completion of our staff study of Section 22(d). The Commission has recently been asked to consider rule changes which would result in lower administrative costs on payroll deduction plans and other

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1/ Securities Act Release No. 5248, May 9, 1972

2/ Investment Company Act Release No. 5507, October 7, 1968

voluntary plans for accumulating mutual fund shares by means of periodic small purchases. These rules now require that shareholders receive individual notices, confirmations, dividend statements and shareholder reports. Our staff is exploring whether these rules can be revised without diminishing the basic shareholder protections they provide as well as re-examining the earlier grouping proposal and the comments received on it.

Issues to be considered

A. Repeal of Section 22(d) of the Act

1. Complete Repeal

The system of retail price maintenance under which mutual funds are distributed tends to raise rather than lower prices. Under it, fund distributors compete for the favor of dealers and salesmen through a system of sales incentives which creates a constant pressure to raise sales loads or reduce the principal underwriter's margin.

The question is whether there is any longer sufficient public interest in the continuation of this system as an exception to the general rule of free competition which prevails in most other segments of our economic life.

2. Partial Repeal

Should retail price maintenance be retained but only for smaller sales, allowing negotiated rates and free competition to prevail on that portion of any purchase in excess of a fixed amount, for example $300,000? Or, should a system of negotiated rates be instituted gradually over a period of time permitting data to be assembled as to the effects of repeal on various segments of the mutual fund market? If such gradual reductions are appropriate, can they be achieved under the Commission's exemptive power or would legislation be needed?

3. Price Competition Within a Limited Range

Should retail price maintenance be retained with respect to a minimum schedule of sales loads, with the statute also specifying a maximum sales load, but allowing for price competition in the range between the specified maximum and minimum loads?

4. A Current Public Offering Price Described in the Prospectus

Section 22(d) states that "no registered investment company shall sell any redeemable security . . . except either to or through a principal underwriter for distribution or at a current public offering price described in the prospectus." Dealers are also required to sell at "a current public offering price described in the prospectus." There is no explicit requirement that there be a single uniform offering price, though that has been the long-standing interpretation of the provision. Would the statute be satisfied if the prospectus described different offering prices for different dealers or in different situations and thus permitted price competition in a manner sanctioned by the investment company itself?

5. Prohibit Price Competition from Non-Contract Dealers

Historically, a principal reason given for the enactment of Section 22(d) was the need to prevent price competition and secondary or "bootleg" markets made by non-contract dealers. Such dealers allegedly undermined the distribution structure by obtaining fund shares from sources other than the principal underwriters and selling them for lower prices than contract dealers could. In this way they could short-circuit the distribution process and destroy the underwriter's ability to promote the fund. Is it desirable or necessary to prevent this and, if so, if Section 22(d) is repealed should the legislation also provide that only contract dealers would be entitled to sell shares at prices other than the current offering price described in the prospectus?

B. Rules Under Section 22(b) and Other Provisions of the Act

1. Lower Breakpoints reflecting the Reduced Cost of Diversification on Larger Purchases

Section 22(b) of the Act gives the NASD and the Commission rule-making authority to prevent mutual funds being sold at a sales load which is excessive. Under that section, as amended, mutual fund sales charges must allow for "reasonable compensation for sales personnel, broker-dealers,

and underwriters, and reasonable sales loads to investors". It is clear that, whether or not Section 22(d) is repealed, mutual fund investors require the protection of a statutory ceiling on sales loads. One of the principles upon which the NASD study was based was that the cost of fund shares should not exceed the alternate cost of a similar investment. One measure of alternate cost used by the NASD's consultants was the round-trip cost of purchasing a diversified stock portfolio. However, on purchases in excess of $5,000 the alternate cost of diversification appears to be significantly less than the load suggested by the NASD rule proposal. Sales in excess of $5,000 accounted for about 70% of the total volume of mutual fund sales in 1970. Should any NASD rules take into account the reduced cost of diversification on purchases above the $5,000 level?

2. Regulation of the Dealer-Discount

The Commission in its Statement on the Future Structure of the Securities Markets expressed its concern over the effect of varying sales incentives available from different funds. In theory there seems to be widespread agreement that it is undesirable to allow an individual salesman to participate in the brokerage generated by an investment company complex whose funds he sells. The same kind of problem exists when fund distributors pay different dealer discounts. When one fund offers a dealer discount of 6 percent and another 8 percent, sellers are invited to recommend the fund that pays them best rather than the one that is best for their client. This practice also contributes to the pressure to raise sales loads or reduce the distributor's margin. Is this an area of concern and, if so, does the Commission have authority to deal with it by classifying as an "underwriter" under Section 2(a)(40) of the Act anyone who receives more than the "usual and customary distributor's or seller's commission" on the sale of mutual fund shares. In the alternative, should the NASD or the Commission take action under Section 22(b) to limit dealer discounts? If dealer discounts should be limited, in what respects?

3. Continuous Discounts

Under existing sales load structures purchasers of large volumes of mutual fund shares receive a volume discount when purchases are made in amounts exceeding specified breakpoints, e.g., $10,000, $25,000 or $50,000. The reduced charge applies to the entire purchase, not merely to the portion in excess of the breakpoint. This means that for a fund with a basic sales charge of 8.5% which drops to 7.5% on purchases in excess of $10,000 or more, a $9,900 purchase will produce gross revenue of $841.50 for the selling organization. If the purchase were $100 greater, i.e., $10,000, total selling compensation drops to $750. Such a system discourages sellers from alerting prospects to the economies produced by breakpoints and places ethical strains on dealers and salesmen. Should Rule 22d-1 be amended to require that volume discounts be provided only where continuous schedules are in effect under which reductions fall only on that portion of the order in excess of the breakpoints?

4. The Value of Additional Product Features

The NASD Study suggests that the maximum load be determined by the value of the product and that only those funds which offered certain product features -- dividend reinvestment at net asset value, lower breakpoints for volume discounts and dividend reinvestment at net asset value -- should charge the maximum loads. Is this a desirable approach in the light of the fact that a significant proportion of investors do not take advantage of these features? Is this approach desirable assuming a system of continuous discounts?

5. Contractual Plans

The total sales loads on contractual plans and the breakpoints on such plans are higher than the typical loads and breakpoints on mutual funds generally. The effective load on contractual plans may be significantly higher when the effects of lapses and persistency is taken into account. Is it premature at this time to take any action with respect to maximum sales charges applicable to contractual plans in light of the changed conditions in which the plan industry now operates, and in view of the protections afforded to contractual planholders by amended Section 27 of the Act?

C. Further Liberalization of Advertising Rules

1. Advertising

Advertising, an effective and a relatively low-cost method of conveying information to prospective purchasers, has been confined to a minimal role in the marketing of investment company securities. Restrictions on advertising have made it difficult for the mutual fund industry to tell its story through the mass media. The Commission recently liberalized its rules with respect to the advertising of investment company securities. What further liberalization would be in order? Is legislation necessary in this area?

2. Statement of Policy

The Statement of Policy which governs investment company advertising and sales literature has not been amended since 1957. A number of its basic approaches have been questioned over the years. These include limitations on projections, use of mountain charts to convey cumulative performance, prohibitions against a total yield approach, absence of data upon which to base conclusions as to average annual performance and variability of performance from year to year. To what extent are these elements of the Statement of Policy no longer appropriate?

D. Simplified More Readable Mutual Fund Prospectuses

Advertising restrictions rest on the premise that the statutory prospectus will be the key selling document. However, selling practices typically relegate the prospectus to a secondary role and very often legal requirements result more in confusing the ordinary investor than assisting him in reaching an informed judgment. The Commission has designated an Advisory Committee to make suggestions with respect to this and related subjects. Assuming simple clear prospectuses geared to the ordinary mutual fund investor's needs, will the prospectus be used more extensively and earlier in the distribution process and will this affect selling?

E. Group Sales

Mutual fund sales charge schedules provide for quantity discounts on larger orders. But the Commission's rules under section 22(d) preclude the grouping or pooling of orders for the purpose of obtaining such discounts. Has this anti-grouping rule, which superseded contrary administrative positions, outlived its usefulness?

F. Reducing Paperwork in Small Transactions

Payroll deduction plans and other voluntary plans for accumulating mutual fund shares by means of periodic small purchases appear to offer great potential. Some of the present rules under the federal securities laws make such plans expensive. The rules in question require that each fund shareholder receive such individual notices and services as individual confirmations, dividend statements and shareholder reports. To what extent can the Commission amend these rules to achieve lower costs on small transactions without diminishing the basic investor protections they provide?

G. No-Load Sales

Under present administrative interpretations brokers and dealers have no direct incentive to recommend "no-load" funds, i.e., funds that sell their shares directly to the public free from any sales charge. The imposition of any charge for recommending the shares or for effecting the purchase of such a fund, especially if the fund encourages or has knowledge of the practice, has been viewed as an impermissible deviation from the prospectus representations as to no-load status as well as a violation of Section 22(d). Should the Commission re-examine its present administrative interpretations in order to remove disincentives operating against recommending no-load funds? Should it permit brokers and dealers to charge a normal stock exchange commission for recommending and effecting an investment in a no-load fund?

H. Development of An Adequate Economic Data Base

If mutual fund sales charges are to be regulated, reliable data as to the industry's costs, profitability, and general economic structure is necessary. Such data should be available on a continuous basis so as to enable the regulators to monitor trends, thus avoiding the undue regulatory lag that has plagued other types of regulation. Is it possible to develop a system of cost allocation and other accounting procedures necessary to provide such data in a meaningful fashion? What burdens would be involved in moving the industry to such a uniform system?

Procedures

The policy implications of these and other related questions are of great significance to the securities industry generally and particularly to investment companies, their principal underwriters, the broker dealers and salesmen who distribute them, and to the investing public. Accordingly, all persons interested in, affected by or concerned with the distribution of investment company shares and the role of investment companies in the securities markets are invited to provide their views to the Commission with respect to all such issues.

The proposed public hearings will be policy making proceedings. They are designed to give the Commission further insight into the major issues and alternatives facing the industry in the area of mutual fund distribution in order that the Commission may formulate its own legislative recommendations, propose new rules and amend existing rules to the extent appropriate under its present authority. Of course, as in so many areas of the securities laws, the issues are largely interrelated and actions in one respect may deeply affect others. Thus, the full impact of a particular rule or legislative change may be difficult to gauge and all of the questions raised will not be resolved definitively at one time.

These hearings are concerned with the formulation and establishment of policy and the rules necessary to implement it. The procedures will be tailored to this end. Because of the wide ranging scope of the inquiry it appears appropriate and expeditious to require written submissions in the first instance. Comments should be addressed to the enumerated questions or other relevant issues the commentator may care to call to the Commission's attention. Persons commenting may feel free to submit any relevant data or other information relating to these issues, and reference may be made, where appropriate, to the Commission's Staff Study, the NASD Study, to prior hearings, policy statements or testimony. All such submissions will be available for public inspection. After the Commission has had a chance to review all submissions, brief oral statements will be invited from among those who have made submissions and requested to be heard. Persons making oral presentations should be prepared to respond to inquiries from the Commission and its staff.

Interested persons are requested to submit their views, any data or other comments or information in triplicate, to Allan S. Mostoff, Director, Division of Investment Company Regulation, Washington, D.C. 20549, no later than December 6, 1972. All such material should be designated "Mutual Fund Distribution Hearings", File No.4-164.

By the Commission.

Ronald F. Hunt
Secretary

M. Parrillo

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

RECEIVED

December 5, 1972

ATTENTION OPERATIONS OFFICERS

NASD REGULATION

To: All NASD Members

Re: First Midwest Investment Corp.

The NASD's Uniform Practice Committee has been advised that a SIPC Trustee has been appointed for First Midwest Investment Corp., of Milwaukee, Wisconsin. The Committee has determined that members may use the immediate close-out procedures under Section 59(h) of the Uniform Practice Code for open transactions with the above named firm.

Please refer to Section 59(h) of the Code for the detailed procedures.

All money differences and other matters of business should be taken up with the below named individual:

For: First Midwest Investment Corp.
1112 North Jackson Street
Milwaukee, Wisconsin 53202
Telephone: (414) 276-9900

Trustee: Frank C. Verbest
(can be reached through the firm)

Questions regarding this notice should be directed to the Member Operations Department, 2 Broadway, New York, New York 10004 (212) 269-6393.

Sincerely,

John S. R. Schoenfeld

John S. R. Schoenfeld
Executive Vice President

M. Parrillo

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 6, 1972

NOTICE

TO: All NASD Members

RE: Recent Amendments to SEC Rule 17a-5

Introduction

Important rule amendments to SEC Rule 17a-5 under the Securities Exchange Act of 1934 and the related audit requirements of Form X-17A-5 became effective on September 30, 1972. As amended, the rule now requires the sending directly to customers of broker-dealers certain information which the Commission feels essential for a customer to have in order to judge whether his broker-dealer is financially sound and able to efficiently and safely handle his securities transactions, monies, and securities. The amended rule will also require that a complete set of financial statements be furnished to the Commission in addition to Form X-17A-5. This latter requirement, however, becomes effective for calendar and fiscal years ending on or after December 31, 1972.

Additionally, another recent amendment, adopted effective October 15, 1972, requires that each report filed pursuant to Rule 17a-5 containing statements of financial condition dated on or after October 16, 1972, must be accompanied by a supplemental report on the status of the membership of a broker-dealer in the Securities Investor Protection Corporation.

In order to assist members in meeting their responsibilities under these recently adopted amendments, the Association is taking this opportunity to review the major changes in the requirements of Rule 17a-5.

Statements to be Furnished Customers - Quarterly

As mentioned above, each subject broker-dealer is required to furnish his customers with certain information concerning his firm's financial condition on a quarterly basis. Such information must include an uncertified balance sheet and a statement of the firm's net capital and required net

capital computed in accordance with the net capital rule to which the member is subject, together with an explanation thereof.

In this connection, the following illustration has been prepared as a guide to members in developing the explanation required by this amendment. Inasmuch as this is a general example, it is not intended to be all-inclusive and the question of adequate disclosure in a given case may require more detailed or substantive information depending upon the particular financial conditions and circumstances of each firm.

> As a registered broker-dealer, firm name, is subject to the requirements of Rule 15c3-1 ("the net capital rule") under the Securities Exchange Act of 1934. The basic concept of the rule is liquidity, its object being to require a broker-dealer to have at all times sufficient liquid assets to cover his current indebtedness. Specifically, the rule prohibits a broker-dealer from permitting his "aggregate indebtedness" from exceeding twenty [1/] times his "net capital" as those terms are defined. On date, firm name's aggregate indebtedness and net capital were $_____ and $_____ respectively, a ratio of ____ to ____. As calculated by us, firm name's required capital for this same date was $_____. Firm name has at all times during the past year been in compliance with the net capital rule of the SEC and its ratio of aggregate indebtedness to net capital has not exceeded ____ to ____. [2/]

The balance sheet and net capital statements required by the amended rule must be furnished to customers not later than forty days after the end of either a calendar quarter, a fiscal quarter, or a quarter in which Form Q or the Joint Regulatory Report is filed. With respect to the three options available under this rule, it should be noted that the data required to be furnished customers can be readily obtained from the NASD Quarterly Financial Report. Since the Form Q provides an excellent format for fulfilling these requirements, the Association recommends that the date selected

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1/ During the first year of operation, the ratio requirement for each broker-dealer registered with the Commission on or after August 13, 1971, is 8 to 1. In this connection, members subject to an 8 to 1 requirement should substitute the word "eight" for "twenty" in the above legend.

2/ If a member has not at all times during the past year been in compliance with the SEC Net Capital Rule, he must fully disclose such facts to his customers.

by a member for compliance with subparagraph (n) of the amendments to Rule 17a-5 coincide with the Form Q period ending date. In this regard, the Commission has advised that once a particular quarterly filing period is chosen, a member must continue to send future statements on the same basis. Hence, a shift from a calendar to fiscal quarter, for example, is not permitted except with valid justification.

It should be noted that the balance sheet and net capital statement need not be furnished to each customer of a broker-dealer, rather they must be furnished to those customers falling within the definition of that term in the rule. For purpose of this rule, the Commission has defined "customer" to include:

a. Any person for or with whom a member has effected a securities transaction in a particular month. (In this regard, a member can distinguish the month required as being either the month of the balance sheet date or the month following the balance sheet date. For example, if a member determines to furnish customers with financial data as of December 31, 1972, such reports could be sent to those customers who effected a securities transaction during either the month of December or January. However, once this selection is made, each subsequent customer list must be determined in the same manner); and,

b. Those persons for whom the member carried a free credit balance or for whom the member held securities for safekeeping or as collateral during the month determined by the member per paragraph (a) above.

It is also important to note that the quarterly information sent to customers need not be certified.

The amendments also require that the material furnished customers be filed concurrently with the Commission, the NASD and each national securities exchange to which a member belongs. In this connection, material required to be filed with the Association should be sent to the NASD, 1735 "K" Street, N. W., Washington, D. C. 20006, to the attention of the Regulation Department, and may be included with the Form Q filing.

Additional Statements to be Furnished to the Commission

In addition to the above requirement, members who file an X-17A-5 report for calendar and fiscal years ending on or after December 31, 1972,

must file with the appropriate Regional Office of the Commission the following material:

a. A balance sheet based on the X-17A-5 report;

b. A statement of income;

c. A statement of source and application of funds;

d. A statement of changes in subordinated accounts; and,

e. A statement of changes in sole proprietor's capital or the aggregate of partner's capital accounts or each component of corporate stockholders' equity for the period since the date of the immediately preceding report filed pursuant to SEC Rule 17a-5.

Statements to be Furnished Customers - Annually

Concurrent with the above requirement, each member must send to customers the following:

a. An unconsolidated balance sheet with appropriate notes including but not limited to the nature, amounts and maturities of subordinated capitalization. This balance sheet must be certified unless such requirement is waived by a specific exemption.

b. A statement indicating the amount of the firm's net capital and its required net capital, computed in accordance with Rule 15c3-1 or the net capital rule of the national securities exchange to which the firm is subject. As noted above, a statement explaining net capital must be included.

c. If in connection with the most recent report on Form X-17A-5 the independent accountant commented on any material inadequacies found to exist in the accounting system, the internal accounting control, procedures for safeguarding securities, or the procedures followed in complying with Rule 17a-13, there must be a statement by the firm that a copy of the report is currently available for the customer's inspection at either the office of the Commission in Washington, D. C., the Regional Office of the Commission or at the firm itself.

d. A statement indicating that Part I of the most recent annual report of the firm on Form X-17A-5 is available for examination and copying at the principal office of the firm and also at the appropriate Regional Office of the Commission.

Exemptions

Certain members of the Association are exempt from these recently adopted provisions to Rule 17a-5. Each member should carefully review the exemptive criteria in order to determine if the provisions are applicable to their particular organization. Briefly, members who are exempt from these requirements include:

a. Firms who are unconditionally or on specific terms and conditions exempt from Rule 15c3-1 (the net capital rule) pursuant to the provisions of subparagraph (b)(3) thereof;

b. Firms who meet the conditions for maintaining minimum net capital of $2,500 as per subparagraph (a) of the net capital rule;

c. Firms who introduce all customer accounts to a clearing member on a fully disclosed basis. (In this arrangement the clearing member must reflect all transactions of the introducing firm on its books and records in accounts it carries in the names of these customers. The clearing firm thus assumes the responsibility of furnishing these customers the reports required by these amendments. Under this arrangement the introducing firm must not hold funds or securities for or owe funds or securities to customers other than funds or securities promptly transmitted to the clearing member. Any deviation from the above description would nullify this exemption); and,

d. Firms who are exempted from the provisions of the SEC Rule 17a-13, "Quarterly Security Counts to be Made by Certain Exchange Members, Brokers and Dealers". In this regard, it is suggested members review paragraph (a) of that rule for description of the exemption provisions.

Supplemental Report and Independent Public Accountant's Certification Respecting Status of Member's SIPC Membership

Since certain discrepancies have been discovered between data received by the Commission and SIPC concerning the figures upon which SIPC assessments are based, the Commission has adopted this amendment to provide that SIPC assessment reports be examined by independent accountants. Therefore, reports filed pursuant to Rule 17a-5, which include statements of financial condition dated on or after October 16, 1972, must be accompanied by a supplemental report and a certification of the independent public accountant on the status of the firm's membership in SIPC. As determined by the Commission, this supplemental report shall cover the SIPC annual general assessment reconciliation or exclusion from membership forms. The following information must be included in the supplemental report:

a. A schedule of assessment payments which must show any overpayments applied or carried forward. In this regard, members should denote such overpayments by referencing payment dates, amounts, and the name of the SIPC collection agent who received such payment.

b. If a firm claims exclusion from SIPC membership, a statement noting exclusion from such membership under Section 3(a)(2) of the SIPC Act of 1970 must be made a part of a broker or dealer's filing. If a firm files an exclusion statement, the date and name of the SIPC collection agent with whom a Certification of Exclusion from Membership (Form SIPC-3) must be made a part of such statement.

c. An accountant's certificate which states his opinion that either the assessments were determined fairly in accordance with applicable instructions or forms or that a claim for exclusion from SIPC membership was consistent with a firm's reported income. If an accountant's review did not provide the basis for issuing such a certification, the accountant must state the extent of his review. In this regard, the Commission outlines six minimum procedures for an accountant to follow in the conduct of such review.

d. The Commission has determined that this supplemental report should be in letter form addressed to the Commission and should be filed concurrently with the report

filed pursuant to Rule 17a-5 in triplicate original, manually signed, dated and bound separately. The accountant's report should be filed as an attachment to the firm's supplemental report. Association members should note that there are no exemptions to this amendment. Therefore, each firm who is required to file a report pursuant to Rule 17a-5 must also file the SIPC supplemental report.

The above summary is intended to highlight the major components of these amendments. Consequently, each NASD member should review both SEC Release No. 34-9658, Amendments to Rule 17a-5 Under the Securities Act of 1934 and Related Audit Requirements of Form X-17A-5, and SEC Release No. 34-9766, Amendment of Rule 17a-5 Under the Securities Exchange Act of 1934 Concerning Report of Securities Investor Protection Corporation Assessments by Adoption of Subparagraph (b)(4). These releases present the complete text of these important amendments.

Questions pertaining to the Rule 17a-5 amendments may be directed to Gerard F. Foley at (202) 833-7320.

Sincerely,

Gordon S. Macklin
President

GSM:msb

Mr. Parrillo

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 8, 1972

ATTENTION OPERATIONS OFFICERS

To: All NASD Members

Re: Horizon Securities, Inc.
295 Madison Avenue
New York, New York 10017

The NASD's Uniform Practice Committee has been advised that a SIPC Trustee has been appointed for Horizon Securities, Inc., of New York City. The Committee has determined that members may use the immediate close-out procedures under Section 59(h) of the Uniform Practice Code for open transactions with the above named firm.

Please refer to Section 59(h) of the Code for the detailed procedures.

All money differences and other matters of business should be taken up with the below named individual:

Alan Palwick, Esq.
Burns, VanKirk, Jube & Kafer
521 Fifth Avenue
New York, New York 10017
Telephone: (212) 972-0500

Questions regarding this notice should be directed to the Member Operations Department, 2 Broadway, New York, New York 10004, (212) 269-6393.

Sincerely,

Lee C. Monett

Lee C. Monett
Vice President
Member Operations

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 11, 1972

ATTENTION OPERATIONS OFFICERS

To: All NASD Members

Re: Comstock Securities Limited
225 South 2nd E.
Salt Lake City, Utah 84111

The NASD's Uniform Practice Committee has been advised that a SIPC Trustee has been appointed for Comstock Securities Limited, Salt Lake City, Utah. The Committee has determined that members may use the immediate close-out procedures under Section 59(h) of the Uniform Practice Code for open transactions with the above named firm.

Please refer to Section 59(h) of the Code for the detailed procedures.

All money differences and other matters of business should be taken up with the below named individual:

Herschel J. Saperstein
800 Deseret Building
315 E. 2nd South
Salt Lake City, Utah 84111
Telephone: (801) 364-7831

Questions regarding this notice should be directed to the Member Operations Department, 2 Broadway, New York, New York 10004 (212) 269-6393.

Sincerely,

Lee C. Monett

Lee C. Monett
Vice President
Member Operations

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 15, 1972

TO: NASD Members and Branch Offices

FROM: Gordon S. Macklin, President

RE: New National List Criteria

In a letter of October 27, 1972, you were apprised of the Association's deep concern over the need for newspapers to expand their quotation coverage of securities included in the NASDAQ System. It was pointed out that most newspapers, at the present time, cannot expand their lists to provide quotation coverage to all deserving issues in NASDAQ, and that the NASD was, therefore, studying alternative steps which it might take to restructure the National List to sharpen reader interest in the List throughout the country.

After further study and discussion of the situation by the Association's Board of Governors, the Association announced plans for revision of the List and solicited the views of NASDAQ issuers, the public and the securities industry. Prior to announcement the general plans were discussed with the Securities and Exchange Commission staff and made known to the Commission. The Commission offered no objection to the Association's general plan in this area. After the comments were received a specific approach was informally submitted to the SEC staff along with the comments. This approach (a copy of which is attached and presently being voted upon by the Board) is based primarily on trading activity and minimum price. It is hoped that by recommending that newspapers publish quotations lists composed of the most active NASDAQ securities, progress can be made in having newspapers expand their coverage of the NASDAQ market. Progress in this area could allow us to offer many more NASDAQ securities deserved coverage in newspapers all over the nation.

The new criteria are presently being voted upon by the Association's Board of Governors. If adopted, the National List would be divided into two sections. The first section designated the Most Active National List, would consist of the 1,400 most active securities in NASDAQ, determined according to the weighted average weekly volume calculated by the NASDAQ computers and meeting certain minimum price requirements. (See footnote to page 1 of the attached criteria.) This List would

be revised every six months and the NASD, under the contemplated amendments, is suggesting to newspapers that it be published with bid, ask, net change from the previous day, and volume.

The second section designated the Supplementary National List, would consist of the next 900 most active securities which meet minimum price and dollar volume requirements. The NASD is suggesting that the Supplementary National List be published in narrower column widths without the net change or volume in order to accommodate more listings. This List would be revised every two months, enabling issues to be reconsidered frequently.

Starting on January 3, 1973, the WALL STREET JOURNAL plans to publish daily both sections of the National List, or a total of 2,300 securities, compared with approximately 1,700 in the present National Daily List. Further, we understand that the JOURNAL will publish all earnings statements for companies quoted on the Most Active List. For companies included in the Supplementary List, the JOURNAL will carry only the annual report if the security issue is in the List at the time the annual report is released. Dividend declarations and other newsworthy announcements will be carried by the JOURNAL on companies quoted in both sections of the National List. The JOURNAL would like to receive directly from all companies quoted in NASDAQ copies of the annual report and Form 10-K which is filed with the Securities and Exchange Commission. These reports should be addressed to Statistics Department, WALL STREET JOURNAL, 22 Cortlandt Street, New York, N. Y. 10007.

The securities expected to be included in the revised January 1973 National List will be determined on the basis of data in the NASDAQ computers as of December 1, 1972.

As in the past, the NASDAQ System would continue to release to the newswire services the quotations and volume on substantially all of the 3,500 issues in the System so that newspapers would continue to have access to this information on any issue in which they have particular interest. Currently, the FINANCIAL WEEKLY, published by Media General, presents weekly data on quotations and volume for the complete list of NASDAQ securities that are released to the newswire services, and Francis Emory Fitch publishes quotations and volume data on the complete NASDAQ list on a daily basis. The OTC MARKET CHRONICLE published in New York City also carries complete NASDAQ quotations once a week. These publications are mentioned here so that you will be aware of where you may find the complete NASDAQ List. We will continue to make every effort to interest other financial publications in introducing the full NASDAQ List showing quotations and volume on a daily basis.

In addition, the Association will make a concerted effort to have those issues which fall from the National List picked up in local quotations lists in those cities where shareholder concentrations indicate sufficient local interest.

All NASDAQ companies are being individually apprised of any changes which might result from the implementation of the new criteria.

Questions regarding the new criteria should be directed to Mr. William R. Turner, Assistant Director NASDAQ Operations, NASD, 17 Battery Place, New York, N. Y. 10004.

Enclosure

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NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 26, 1972

Important Emergency Notice

To: All NASD Members

The NASD respectfully requests all members to close their business operations on Thursday, December 28, in memoriam to Harry S. Truman, the 33rd President of the United States, who died today, December 26, 1972.

The NASDAQ System and the Exchanges will be closed on Thursday, December 28, 1972.

Sincerely,

Gordon S. Macklin
President

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

December 27, 1972

NOTICE

TO: All NASD Members

RE: Completion of Transactions in Suspended Securities

In recent months the Association has received a number of inquiries from members concerning their obligations to complete transactions in securities which subsequently became the subject of an SEC trading suspension.

In response to similar questions several years ago the SEC issued a release on the subject and stated as follows: 1/

> "A number of questions have been presented recently as to whether, during the period when trading is suspended by order of the Commission pursuant to Section 15(c)(5) or Section 19(a)(4) of the Securities Exchange Act of 1934, a broker or dealer may complete (e. g., by payment or delivery) an agency or principal contract entered into prior to the suspension.
>
> "It is the position of the Division that where the broker or dealer is himself acting in good faith, where he is not connected with the activity announced by the Commission as a basis for suspension pursuant to Section 15(c)(5) or Section 19(a)(4), and where he has no reason to believe that his customer is so connected, no objection need be raised under such sections because the broker-dealer completes his contractual obligations in the particular transaction (e. g., by payment or delivery) while the suspension is still in effect. The Division believes that in each such case, however, he

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1/ Securities Exchange Act Release No. 7920 (July 19, 1966).

should inform his customer, prior to consummating the transaction, that trading in the security is suspended and of the reasons announced by the Commission for suspending trading.

"A broker-dealer, in deciding whether to consummate such a transaction, must of course consider not only the provisions of Sections 15(c)(5) and 19(a)(4) but also all other applicable provisions of the Federal securities laws."

Consistent with this position is the view of the Association that a "contract is a contract" and except that a broker-dealer honestly and with a reasonable basis believes that his transaction with another was part of a fraudulent scheme and that it had justification for refusing to carry out the transaction, a member is obligated to consummate, by payment or delivery, any and all transactions in securities entered into in good faith prior to their suspension.

In connection with a landmark case involving the SEC's review of a disciplinary action taken by the NASD against a member, the Commission remarked that in order for a breach of contract to violate the Association rules, it must appear that such failure was unethical or dishonorable or that the breach was committed without equitable excuse or justification. 2/

Although the Association is not empowered to decide the private contractual rights between parties, it has taken the position that the failure to complete a contract, "in the absence of an equitable excuse or justification", represents a violation of Section I of Article III of the Rules of Fair Practice which requires that a member, in the conduct of his business, observe high standards of commercial honor and just and equitable principles of trade. In a footnote to the case referenced below (Lerner & Co.), the Commission cited an earlier proceeding involving contractual undertakings wherein a former SEC Commissioner commented that, "The deliberate, willful and unjustifiable breach of a valid contract between members of the same association ... is ... neither honorable, just or equitable". 3/ Consequently, the failure of a member to fulfill

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2/ Southern Brokerage Co., Inc., Securities Exchange Act Release No. 7463 (November 19, 1964), p. 5.

3/ In Lerner & Co., Securities Exchange Act Release No. 5538 (June 28, 1957) p. 7, the Commission states that, "We have no doubt that in the absence of justifying or extenuating circumstances a member's failure

his contractual responsibilities, except under the condition described above, may result in the initiation of disciplinary proceedings by the Association.

In a later case, an action taken by the Association for failure to complete a transaction with another member resulted in the censure and fine of the defaulting member for violating Article III, Section I of the Rules of Fair Practice. Upon a petition for review of the NASD order, the SEC dismissed the application and held that respondent had no equitable justification for its refusal to honor its obligation to the other member, and that respondent's conduct was inconsistent with just and equitable principles of trade and contrary to the requirements of Section I, Article III of the NASD Rules. This decision was subsequently upheld by the U. S. Court of Appeals, Second Circuit, in 1965. 4/

In connection with the above, it should also be noted that in addition to the NASD's regular complaint procedures as outlined in the Code of Procedure for Handling Trade Practice Complaints, the Association has adopted a Code of Arbitration Procedure for the arbitration of clearing controversies and securities transactions disputes between or among members, public customers, and others. Members who desire to avail themselves of this procedure should contact Louis Korahais, Director, Arbitration, 17 Battery Place, New York, New York 10004. Telephone: (212) 269-6395.

Very truly yours,

Frank J. Wilson

Frank J. Wilson
Senior Vice President
Regulation

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to live up to contract obligations owed to a customer or a fellow member would constitute dishonorable and inequitable conduct not consistent with "just and equitable principles of trade" as that term is generally employed.

4/ Nassau Securities Service, Securities Exchange Act Release No. 7464 (November 19, 1964); 348 F. 2d 133 (1965).