

NASD

REPORT TO MEMBERS 1977

Chairman's Report

As befits a nationwide organization run by and representing some 2,800 broker/dealer firms, the NASD in 1977 increased its efforts to help develop a National Market System. Our Board of Governors believes such a system to be inevitable, necessary and desirable.

Throughout 1977, the Association continued to put into practice what it had proposed in its April 1976 *Discussion Paper on Three Issues in the Development of a Central Market System*: (1) the reduction of regulatory overlap and duplication, and progress toward a sole self-regulator for the securities industry; (2) the adaptation of NASDAQ facilities to the requirements of a National Market System; and (3) the establishment of a single national clearance and settlement system for all securities, OTC and listed.

Toward the end of the year, the Association went beyond these specifics and offered its services as a coordinator to the industry and the SEC on the overall design, construction and operation of a National Market System.

Regulatory Responsibility

A National Market System would require a responsive and efficient regulatory atmosphere. During 1977, the NASD and the Boston, Cincinnati, Midwest and Pacific Stock Exchanges signed agreements under which the Association would exercise inspection, examination and enforcement functions for most dual members of the NASD and these exchanges. Also, the NASD would perform registration and recordkeeping functions connected with the dual members.

These regulatory agreements were nearing SEC approval at the end of the year. If approved, they should reduce the regulatory burden in many members' offices and save the industry time and money.

Trading Facilities

"The trading facility of a National Market System is generally viewed as a system of communications by which the various segments of the marketplace, both listed and over-the-counter, are electronically tied together," the *Discussion Paper* observed. In early 1977, the Association took a major step toward this relationship by inaugurating the Consolidated Quotations Service (CQS) on NASDAQ. CQS shows quotations on all New York



Stock Exchange listed securities released by participating exchanges and Third Market makers. Thus it allows subscribers to NASDAQ and CQS to see on the NASDAQ screen the various markets in the country for nearly 2,600 OTC and 1,600 NYSE securities.

Work has begun to expand CQS in 1978. Quotations for American Stock Exchange and regional stock exchange listed securities on CTA Tape B will be added; last sale information for both CTA Tape A and Tape B securities will be shown; and there will be display of size for CQS securities, if the proposed SEC rule requiring it becomes effective.

Thus in 1978 NASDAQ and CQS will become a comprehensive source of information on some 5,300 OTC and listed securities and help tie together the OTC market and all the exchanges.

Third Market Surveillance

CQS on NASDAQ is being prepared to become a regulatory as well as an information tool, in anticipation of increased Third Market trading volume when off-board trading restrictions on listed securities are removed. NASDAQ computers are being programmed to compare CQS quotations with data from NASDAQ's Third Market Transaction Reporting System and to signal unusual price and volume activity in the off-board trading of listed securities. In the Association's view, this and other NASD surveillance capabilities are adequate to govern off-board trading and eliminate the need for additional rules in this area.

Clearing Consolidation

A third component of a National Market System is, in our opinion, a single national clearance and settlement system. Toward this end, the NASD in 1977 consolidated its wholly-owned clearing facility, the National Clearing Corporation (NCC), with the clearing corporations of the New York and American Stock Exchanges into the National Securities Clearing Corporation (NSCC).

The progress of the consolidation has been slowed by legal and other obstacles, which we are hopeful will be overcome in 1978. When we are successful, many dealers in various sections of the country will gain access to a single clearing system, which will mean lower costs and better services than are now available. Competition be-

tween dealers will become more effective, and investors and issuers will also benefit.

The NASD Offer to the SEC

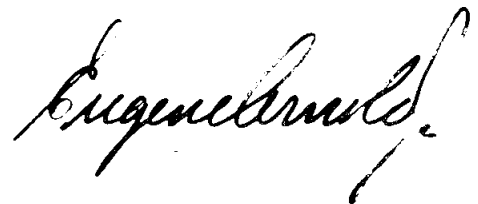
In addition to its concrete contributions toward a National Market System in the areas of regulation, trading and clearing, the NASD in late 1977 offered to act in a coordinating role, for all interested parties, in the development of the System as a whole. At the August 1977 SEC hearings on off-board trading restrictions, SEC Commissioner John R. Evans inquired whether the NASD might be willing to play such a part; Congressmen John E. Moss and Bob Eckhardt endorsed the idea; and the Association responded affirmatively, first by a resolution of the Board of Governors and then by a formal letter to SEC Chairman Harold M. Williams.

To the Members

Underlying the Association's 1977 contributions toward a National Market System was its continuing work on the strengthening of the OTC Market as a vital element of the nation's securities markets. That effort is described in the body of this Report to Members.

Hundreds of people from our member firms contributed to the Association's efforts in 1977. We have all been ably assisted by a seasoned staff of excellent men and women. I am grateful for the cooperation and dedication of everyone, and am confident that the challenges of 1978 will result in further beneficial accomplishments by your organization.

Respectfully submitted,



Eugene Arnold, Jr.

President's Report

In spite of the uncertainty reflected in most financial markets, 1977 was a good year in the over-the-counter market and at the NASD. In contrast to the sharp decline in the Dow Jones Industrial Average, the NASDAQ Composite Index was up 7.3%. Out of the seven different NASDAQ indexes, six recorded increases for the year. Volume in the NASDAQ System totalled 1.932 billion shares for the year versus 653 million shares on the American Stock Exchange and 5.274 billion shares on the New York Stock Exchange. Compared with the previous year, NASDAQ volume showed an increase of 14.7%, while there was an increase of .7% on the American Stock Exchange and a decrease of 1.6% on the New York.



NASDAQ Rebate

Operating data from the NASDAQ System reflects this increase in investor interest. The average number of market makers per security increased from 6.5 to 7.6 during the year. The number of Level 2 and 3 terminals in use increased to 1,099, a gain of 38. In addition, the number of Level 1 terminals receiving NASDAQ information totaled 34,680 at year's end, an increase of 9.3%. This increased level of activity was reflected in the financial results of our subsidiary, NASDAQ, Inc., whose Board of Directors authorized a rebate of \$1,000,000 to System subscribers.

AutEx Agreement

The year saw other reductions in industry costs which were, at least partially, the result of the Association's activities.

In recognition of the growing interest by many Association members in block trading, the NASD announced a cooperative agreement with AutEx in March of 1977. Under this agreement, the Association will receive significant regulatory information from the AutEx system and AutEx service will be made available to small- and medium-sized Association members on a more economical basis. If there is sufficient subscriber interest, AutEx information can be made available on NASDAQ terminals.

Assessment Decreases

During its review of the Association's finances and the budget for 1978, the Board of Governors for the second consecutive year authorized a decrease in the rate of assessment on member income. The rate which was .3% two years ago and .25% last year on gross income from corporate securities was reduced to .21%. The rate on municipal securities was reduced from .2% to .17%. In spite of the reduction in assessment rates and the \$1,000,000 rebate for NASDAQ subscribers, the Association's financial condition was strengthened and liquid reserves for possible changes in business conditions and NASDAQ System enhancements are significant.

Late in the year the Board of Directors of SIPC approved a substantial revision in its assessment schedule which calls for a reduction from .5% to .25% of member gross income for the two quarters ending June 30, 1978. The assessment will then be suspended for the remainder of the year. In January 1979, the assessment will be further reduced to the lesser of \$25 or 1% of a member's gross revenues from the securities business for 1979 and subsequent years. These significant reductions in SIPC assessments are a fine tribute to SIPC's effective and conservative management and also reflect the efforts of the self-regulatory organizations, including the NASD, to upgrade the effectiveness of their surveillance programs during the past five years.

Securities Distribution Rules

For 1978 we see a number of major opportunities and challenges. Foremost on our list of challenges is the need to address the questions raised by the SEC and certain court cases relating to our rules affecting underwritten distribution of securities. At its worst, this threat could materially alter our industry's methods for distributing securities. Such a major alteration may seriously threaten the ability of many corporations to raise capital.

In addition to the efforts related to a National Market System mentioned in Gene Arnold's Report, the Association will be working on many other major projects. Prominent among these are the NASDAQ options program, expanded use of our automated member registration file and a pilot program for selected qualification examinations. This program, in its initial stage, will require candidates for certain qualifications examinations for registered principals to take the test on a cathode ray tube rather than with pencil and paper. This computerized examination offered through the Control Data Corporation's PLATO System will, if successful, add greatly to the members' flexibility for scheduling examinations, eliminate the time required to grade a test and enhance the security of the bank of test questions. If the pilot works well, member savings from an expansion to cover other tests would be significant.

The many special programs and projects, when combined with the Association's regular duties, strongly indicate that the new year will indeed be a busy one. As in the past, hundreds of industry volunteers working on the Board and its many committees will be directing the Association's activities. We have every reason to believe their efforts will produce meaningful results.

Respectfully submitted,



Gordon S. Macklin

1977 REPORT TO MEMBERS

Membership

Members, Branches, Registered Representatives

During 1977, the number of Association member firms was reduced by 3.6%, from 2,877 at the beginning of the year to 2,772 at its end. However, the number of branches of the members rose by 3.3%, from 5,949 to 6,144. The number of registered representatives showed a nominal increase from 190,862 to 191,786. Thus 1977 was a year of relative membership and registration stability.

Among the larger firms, 12 mergers of two each and one of three resulted in a membership reduction of 14. Major objectives of the mergers were diversification and economy of scale.

Among smaller firms, the membership reduction was 91. On the one hand, 264 firms terminated their membership, principally because of declining profitability; on the other, 173 new firms joined the NASD for the first time.

(For regional data on members, branches and registered representatives, see Pages 28-32 of this Report.)

Membership Communications

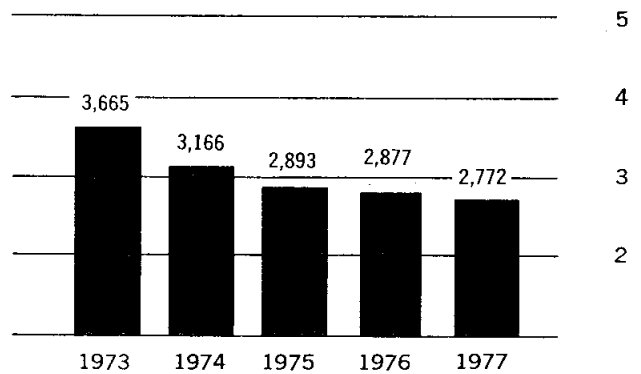
To keep the membership informed of regulatory developments and to solicit members' views on them, the Association published 52 Notices to Members, on matters as routine as settlement dates and as complex and critical as proposed changes in the rules governing securities distribution practices. It also published four issues of the *NASD Newsletter*, with a circulation among registered principals and representatives of 45,000.

Meanwhile, the District Committees across the country pursued Membership Communications Programs responding to local interests and needs. They conducted 57 group meetings attended by

1977 STATISTICAL REVIEW

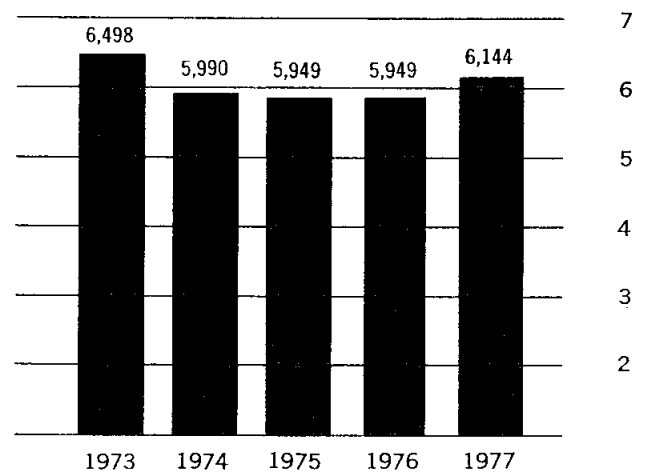
MEMBER FIRMS

Thousands



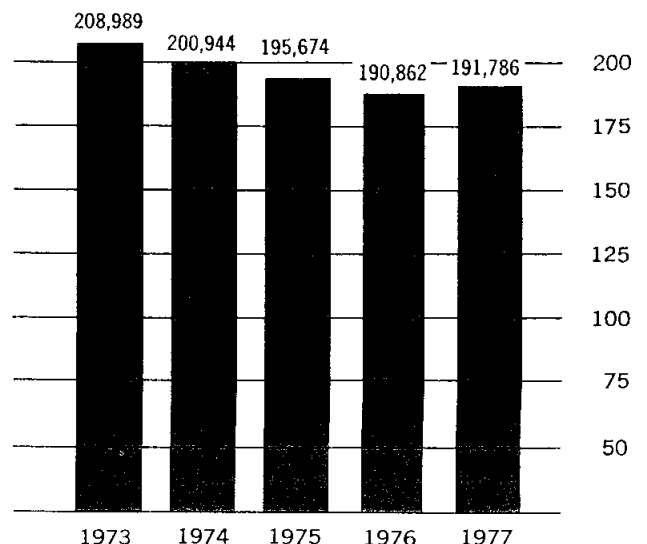
BRANCH OFFICES

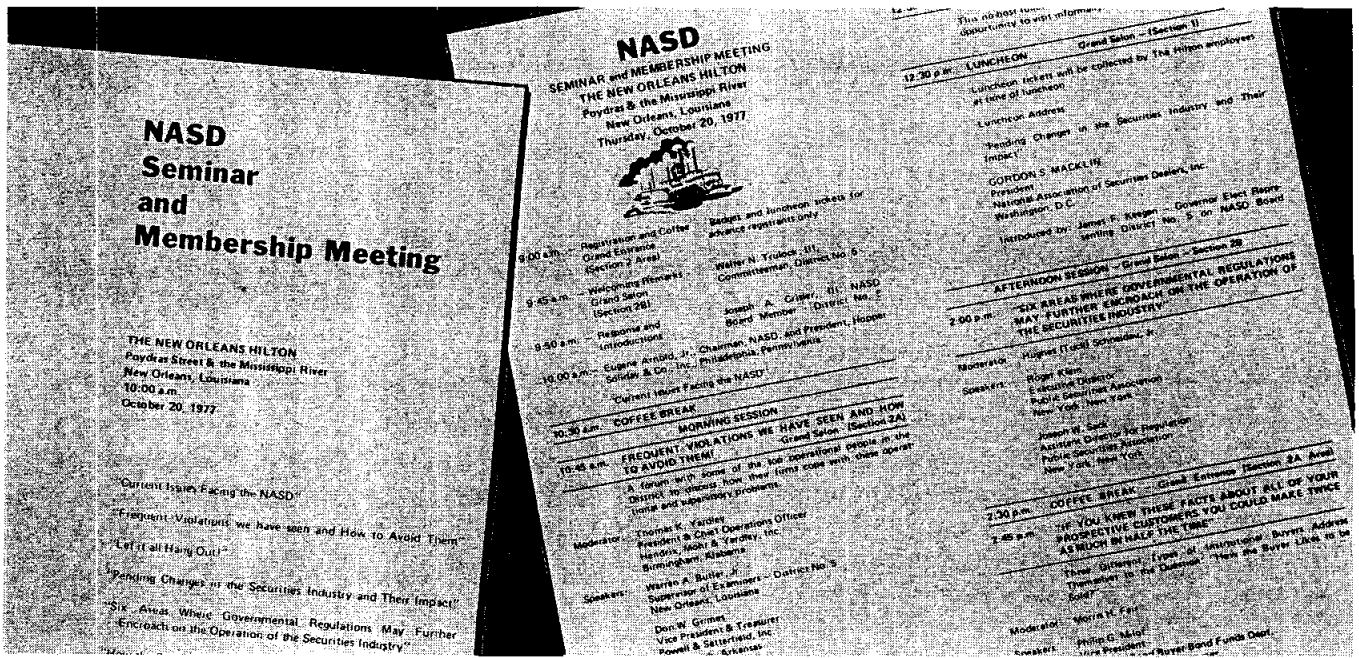
Thousands



REGISTERED REPRESENTATIVES

Thousands





As part of its Membership Communications Program NASD District No. 5 conducted an all-day session in New Orleans.

1,711 persons representing 762 firms. Agendas included:

- Workshops for operations personnel;
- Seminars for financial principals;
- Seminars and workshops on municipal securities regulation;
- Reviews of current issues affecting insurance company and investment company members;
- Discussions of SEC proposals on the resolution of investor disputes and on confirmations;
- Reports on the evolution of the National Market System; and
- Policy recommendations from the membership for consideration by the Association.

Many District Committees will establish Subcommittees to give still more scope and structure to their Membership Communications Programs in 1978.

Administrative Services

In its administrative services to the membership, the Association in 1977 gave special attention to three areas: fingerprinting, the provision of firm rosters and the development, for 1978, of a "one-window" system for registration and examination matters.

Fingerprinting

The Registration Section has processed for the members some 73,000 of the fingerprint record cards required of securities industry personnel by an SEC rule. Also, the names of the persons

fingerprinted were supplied to their employer firms, so that the firms would know the status of their compliance with the rule.

Firm Roster Program

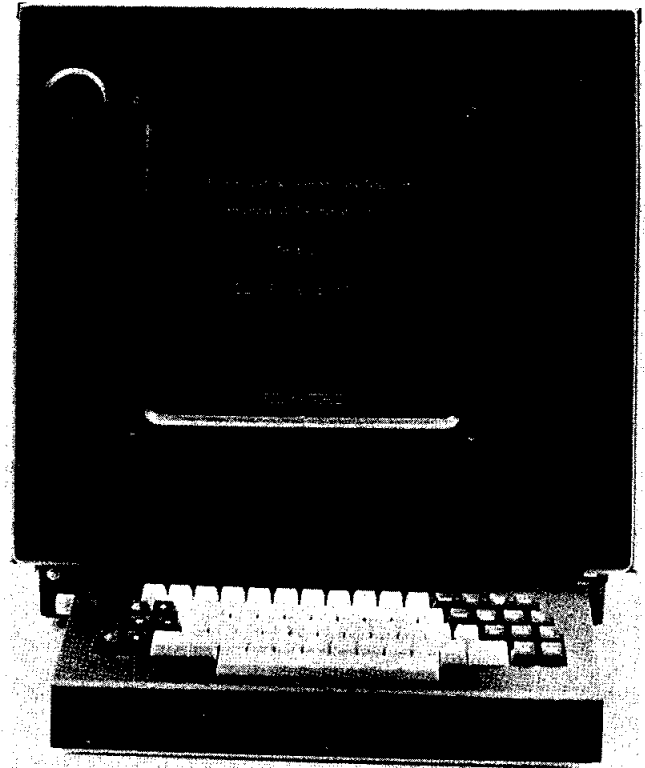
Through the Association's Automated Registered Representative System (ARRS), it has been possible thus far to submit to nearly 1,200 member firms rosters of their employees, with their registration status as shown in ARRS. These rosters help in the updating of members' records and in the elimination of discrepancies between the records of the members and the Association. Many acknowledgements of the usefulness of the firm roster program have been received.

"One-Window" System

In an extension of the firm roster program, the Registration Section has been reorganized to provide member firms with "one-window" service in 1978. Each firm will be able to communicate with a single supervisor in the Section for: (1) the processing of registration applications and terminations; (2) a new service, the conditional approval of a transfer of the registration of an individual from one NASD member to another; and (3) the issuance of test admission certificates and grade notifications for NASD examinations.

It is anticipated that this "one-window" system will increase the personalization, speed and accuracy of administrative services to the membership.

In preparation for testing by computer, NASD examination is displayed on Control Data Corporation terminal.



Qualifications and Examinations

Statistics

Qualification examinations administered during the year, for the NASD and for other institutions, totalled 45,039. This represented an increase of 2,946, or 7%, over 1976.

Examinations administered by the NASD for the five-year period 1973-1977 were as follows:

| Year | Qualification Examinations for NASD | Examinations for Other Institutions | Totals |
|------|-------------------------------------|-------------------------------------|--------|
| 1973 | 46,312 | 26,286 | 72,598 |
| 1974 | 26,783 | 21,059 | 47,842 |
| 1975 | 21,487 | 18,812 | 40,299 |
| 1976 | 22,855 | 19,238 | 42,093 |
| 1977 | 23,910 | 21,129 | 45,039 |

New Functions

With the transfer of test administration to the Registration Section, the Qualifications and Examinations Department was reoriented to concentrate on:

- The development of new examinations under the anticipated higher qualification standards of the SEC and the NASD, and the at least quarterly revision of up to 14 different examinations;
- The coordination of Association testing programs with those of other self-regulatory organizations, the SEC and the states, in order to eliminate duplication of requirements; and
- Further exploration of testing at the computer terminals of the PLATO System of the Control Data Corporation. The use of PLATO, which is operated at CDC's learning centers throughout the U.S.,

could permit candidates to sit for their examinations at any time, rather than waiting for scheduled group testing sessions. Also, candidates could receive their grades on the testing terminals as soon as they finish. Further, the security and integrity of the tests would be reinforced, since the computer would shuffle the questions and construct an individual test for each candidate.

Examinations and Surveillance

The Association's examination and surveillance programs in 1977 showed still better compliance by the membership than in 1976, and a continuation of the steady improvement in compliance over the last several years.

Looking toward the future, the Association took two major steps to reduce the regulatory burdens

of the membership: (1) it reduced examination frequency for a large category of firms; and (2) it signed regulatory agreements with several exchanges which, if approved by the SEC, will virtually eliminate the duplicate inspection of dual members of the NASD and those exchanges.

Examinations of Members

Statistics

The Association in 1977 conducted 2,032 routine examinations and 891 financial and operational examinations of members' main offices. It also conducted 402 special examinations. The corresponding statistics for 1976 were 2,056 routine and 876 financial and operational examinations of main offices, and 611 special examinations.

Included in the totals are the routine and special examinations of member firms doing a municipal securities business. The 1975 Securities Acts Amendments named the NASD as the self-regulatory organization responsible for the examination of municipal securities activities of broker/dealers.

The Compliance Record

Members' excellent compliance with the Association's rules and Federal and state regulations permitted the District Business Conduct Committees to file the great majority of examination reports without need for disciplinary action. The District Business Conduct Committees found it necessary to file 221 formal and 9 summary complaints (203 and 2, respectively, in 1976) and to accept 77 Letters of Admission, Waiver and Consent (74 in 1976). These actions resulted in the expulsion of 18 firms (46 in 1976), the barring of 113 individuals (177 in 1976), the suspension of 5 firms (11 in 1976) and the suspension of 62 individuals (77 in 1976).

Reviews of Financial Reports

To detect potential financial and operational problems and to test for compliance with financial responsibility rules, the Association in 1977 subjected over 8,600 FOCUS Reports to computerized editing and reviewed some 3,700 audited annual reports of members. In addition, the District Office staff reviewed 1,800 FOCUS Part I Reports on a monthly basis.

Member Liquidations

In 1977, five firms designated to the Association were placed in SIPC liquidation. These liquidations

resulted during the year in a total outlay of \$1,130,006 in SIPC advances for 1,878 responses from customers making claims for cash or securities against the five firms.

Also in 1977, the Association successfully monitored the self-liquidation of seven of its member firms whose overall exposure to public customers and to the securities industry had totalled \$7,200,000. One firm had overall exposure in excess of \$4,000,000 and required on-site monitoring by the NASD's Self-Liquidation Task Force.

Reduction of Examination Frequency

In 1978, the Association will eliminate the second yearly financial and operational examination of close to 900 NASD member firms. These are firms which clear their own transactions and for which the NASD is the designated examining authority for financial responsibility purposes. However, the annual routine examination of these firms will continue to include the financial and operational examination. The comprehensiveness of the routine examination and the information available from computer-edited FOCUS reports permit the elimination of the second yearly check on the firms' financial and operational conditions.

Elimination of Duplicate Examinations

In 1978, more than 200 members of the NASD who also belong to the Boston, Midwest or Pacific stock exchanges should benefit from the elimination of duplicate examination programs, if the SEC approves agreements signed during 1977 by the NASD and the exchanges. Under the agreements, the NASD would assume regulatory responsibilities—inspection, examination and surveillance—for most of the dual members. The NASD would generally conduct the on-site examinations, financial and operational surveillance and monitoring of required reports, and share its findings with the exchanges. The exchanges would, however, retain full responsibility for surveillance and compliance with respect to trading activities and practices on their floors, and for their members who do not belong to the NASD.

The Association and the exchanges subsequently held a number of meetings to work out the practical details of their proposed reallocation of regulatory duties, so that it could take effect upon SEC approval. If the approval is given, the dual members should save a major amount of the time and manpower effort which they now must devote to several self-regulatory organizations while being examined, and there should be considerable money savings for the industry.

Regulatory Policy

In the broad and longer-range field of Regulatory Policy, the Association in 1977 addressed 10 major issues, among others:

1. SIPC assessment reduction;
2. Investors' small claims resolution;
3. Securities distribution practices;
4. Direct participation programs regulation;
5. Insurance company involvement in self-regulation;
6. Investment company regulation clarification;
7. Municipal securities regulation development;
8. NASDAQ option program development and delay;
9. Off-board trading restrictions; and
10. National Market System development.

SIPC Assessment Reduction

The Association was represented on the SIPC Task Force, which recommended a reduction of the assessments which broker/dealers pay to the SIPC Fund. SIPC members will be assessed $\frac{1}{4}$ of 1% of their gross revenues during the first half of 1978 only, instead of the past $\frac{1}{2}$ of 1% of their annual gross revenues. After 1978, the assessment will be \$25 or 1% of gross assessable revenues, whichever is less. The Task Force found that the reduced assessments will be sufficient to maintain a SIPC Fund large enough to protect investors against losses from possible failures of securities firms.

Investors' Small Claims Resolution

Another recommendation to reduce broker/dealers' costs while still protecting the investing public was made by the Securities Industry Conference on Arbitration. The Conference was organized by the NASD and the New York Stock Exchange and joined by representatives of the public, the other exchanges and the Securities Industry Association. Under the Conference's recommendation to the SEC, investor disputes involving \$2,500 or less would be settled inexpensively and expeditiously by a single arbitrator on the documentary evidence submitted by the parties or, if necessary, at a hearing.

The Conference proposal is an economical and efficient alternative to a 1976 SEC proposal for the creation of a nationwide governmental network of small claims adjusters. At the beginning of 1977, the NASD had appeared before the Commission and strongly opposed the earlier proposal.

Securities Distribution Practices

The Association during 1977 made a major effort of rule revision and interpretation to reinforce Section 24 of its Rules of Fair Practice, which declares that selling concessions in fixed price offerings of securities shall be allowed only for services rendered in their distribution and then only to broker/dealers.

The meaning of the Section was called into question in the case of *Papilsky v. Berndt*, in which the court ruled that a mutual fund customer might recapture a selling concession extended to a broker/dealer who was also investment manager and underwriter for the fund, by a reduction of its investment advisory fee. The court did, however, express some reservation.

After the *Papilsky* decision a number of investment advisers asked the NASD whether its Rules of Fair Practice indeed did permit an investment company to devise a method by which it could recapture selling concessions in underwritten offerings. The Association, through its General Counsel, stated that the recapture of selling concessions by an investment company would be a violation of Section 24.

Following discussions with the SEC, which questioned the Association's position, the Association engaged in extensive work to review current underwriting practices and to formulate specific policy positions. Its proposals were circulated to the membership for comment and discussed with members at meetings in Chicago, New York and Los Angeles. In the light of membership comments, revisions of the proposals were in progress at the end the year.

Direct Participation Program Regulation

The Association in 1977 reviewed for fairness of the underwriting terms and distribution arrangements 651 public offerings of securities in which members intended to participate, with a registered gross dollar value of \$12.1 billion. Direct participation program, or tax sheltered, offerings made up a significant part of the total, with 182 registrations and aggregate dollar value of \$1.8 billion. This was a nearly 53% dollar value increase over 1976 public direct participation program filings. Equity filings, however, differed little from 1976: 469 offerings were registered, with an aggregate dollar value of \$10.3 billion.

Problems encountered with public offerings of direct participation programs led to submission to the membership for vote of a proposed new Section 35 of the Rules of Fair Practice, which would authorize the Board of Governors to promulgate rules for such offerings. This was ap-



SEC Chairman Harold Williams (seated, pointing) and Commissioner Roberta Karmel (seated, center) watch NASDAQ demonstration at NASD office in Washington.

proved by the members and sent to the SEC for its approval. At the end of the year, revisions were being made in the substantive rules to be sent to the membership for comment.

Further problems encountered with private offerings of direct participation programs led, toward the end of the year, to a special study of such offerings made by NASD members. The study is intended to determine whether a regulatory program for private offerings is necessary.

Insurance Company Involvement in Self-Regulation

The nature of variable contracts and their distribution often requires treatment different from that given to other kinds of securities. Also, more than 80,000 life insurance agents are registered with the NASD and many general securities representatives are becoming licensed to sell insurance. These factors made it important in 1977 to involve insurance company members more extensively in self-regulation.

Senior insurance company officials occupied two of the Governorships-at-Large on the NASD Board, made up almost the entire Variable Contracts Committee and served on eight other National Committees of the Association. Also, seven Districts elected insurance company representa-

tives to their District Committees. The expertise of these officers was extensively used in District Business Conduct Committee proceedings and, at the national level, in developing Association positions on such regulatory policy matters as advertising, confirmations and qualifications standards.

Investment Company Regulation Clarification

Investment companies were also represented on the Board of Governors, National Committees and District Committees of the Association. A program of special conferences brought together the principal underwriters of investment companies and Association officers and staff in Chicago, Dallas, Denver, Houston, Kansas City, Los Angeles, Minneapolis and San Francisco. This service program helped the underwriters better to understand NASD regulatory requirements and helped the Association to become more aware of investment company problems.

Municipal Securities Regulation Development

Throughout the year, the Association worked closely with the Municipal Securities Rulemaking Board (MSRB) and the SEC on such aspects of municipal securities regulation as underwriting

practices and the sale of new issues, amendments to the Uniform Net Capital Rule concerning municipal securities, compliance examinations, advertising, uniform practice and qualification examinations.

The examination for Municipal Securities Financial and Operations Principal, developed by the MSRB and the NASD, was approved by the SEC and its administration in NASD testing centers was scheduled to begin early in 1978. The examination for Municipal Securities Representative was filed by the MSRB for SEC approval, and plans call for the NASD to begin administering it in the first half of 1978.

NASDAQ Options Program Development and Delay

The Association filed for SEC approval a proposal for the display of standardized options on over-the-counter and listed securities on the NASDAQ System. However, the Commission imposed a moratorium on the expansion of existing options trading programs and on the establishment of new ones. Later, the Commission proposed a temporary rule to restrict the expansion of options trading and announced disapproval proceedings against any proposed expansion, including the NASDAQ options program.

The Association strongly protested the moratorium and the proposed temporary rule. In its protest, it cited the extensive resources which had been committed to the NASDAQ options program, the work done to assure effective surveillance of NASDAQ options trading and the more deleterious effects of the SEC actions on the NASDAQ options program than on options trading on the exchanges. The NASD submission was under SEC study at the end of the year.

In December, the Association prepared to file proposals to govern the options activities of the so-called "access firms", i.e. firms which conduct a business in exchange listed options but which are not members of the particular exchange upon which the option traded is listed. The SEC gave a favorable preliminary response to these proposals and approval in early 1978 is anticipated.

Off-Board Trading Restrictions

In testimony at the August 1977 SEC hearings on off-board trading restrictions, the Association summarized its position as follows:

"Our interest in these proceedings is directed to the regulation of off-board transactions, which are over-the-counter transactions and thus subject to the regulatory responsibility of the Association. We believe that the protections against over-

reaching which are in place today coupled with what will be in place by January of next year, including a possible amendment to our best execution rule, are sufficient to deal with the potential problems of overreaching and that new rules in this area are unnecessary."

The protections cited by the Association included: "the substantial public disclosure of current market information"; competitive market making in listed securities as an important factor in favorable execution; the existing regulation and surveillance of the over-the-counter market; NASDAQ restrictions on excess spreads; the NASDAQ Market Surveillance Program and the proposed expansion of the program.

National Market System Development

At the SEC hearings on off-board trading restrictions, Commissioner John R. Evans asked whether the Association would be willing to assume a more active role in the development of a National Market System. A letter from Congressmen John E. Moss and Bob Eckhardt encouraged the NASD to consider such a role. After extensive discussion, the Board of Governors at its September meeting then adopted the following resolution:

"The NASD recognizes the need of its membership, should off-board trading restrictions be removed, to execute customers' orders in listed securities efficiently at appropriate prices through interaction with other orders throughout the securities markets. The NASD proposes to take whatever steps are necessary, individually and in cooperation with other organizations in our industry, to enhance existing facilities and systems. If appropriate, it will, with others, design, build and operate new systems and facilities including those necessary for the protection of limit orders. The Association believes this program is consistent with the Securities Acts Amendments of 1975.

"The NASD will seek comments, suggestions, and assistance of all members in this effort."

NASD Chairman Eugene Arnold, Jr. transmitted the resolution to SEC Chairman Harold M. Williams in a letter which also outlined a five-step approach toward the development of a National Market System. Among the steps proposed were the creation of a nine-member policy group, an advisory group on automation systems and the establishment of a corporation to develop the necessary National Market System facilities.

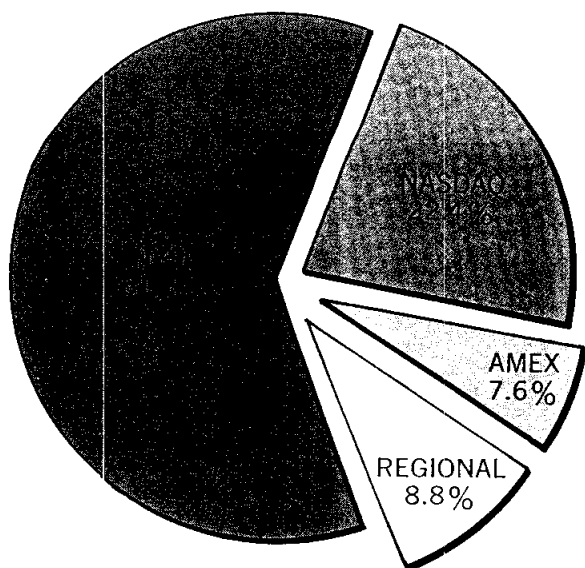
Chairman Williams replied to the NASD that "the Commission will give the approach outlined in your letter the most serious review."

NASDAQ

Major developments relating to the NASDAQ System in 1977 were:

1. High NASDAQ/OTC trading volume and significant rises in the NASDAQ indexes of share prices;
2. Effective response by Market Surveillance to the increased NASDAQ/OTC activity;
3. Additional recognition of the quality of NASDAQ/OTC securities by Federal, state and foreign governments;
4. Increased media recognition of the NASDAQ/OTC market;
5. Expanded NASD communications with NASDAQ companies;
6. Within the NASDAQ System itself,
 - Savings to subscribers,
 - A continued high level of System performance,
 - Major upgrading of System equipment; and
7. Further adaptation of NASDAQ to National Market System requirements.

TRADING ACTIVITY ON NASDAQ AND EXCHANGES



1977 Share Volume

| | |
|-------------------------|---------------|
| New York Stock Exchange | 5,273,767,000 |
| NASDAQ | 1,932,100,000 |
| American Stock Exchange | 653,129,000 |
| Regional U.S. Exchanges | 762,200,000 |

NASDAQ/OTC Market Activity

With 1.932 billion shares traded, volume in the NASDAQ/OTC Market in 1977 was the highest since 1972 and up 14.7% over 1976. Trading averaged more than 7.6 million shares a day compared with 6.7 million in 1976. NASDAQ/OTC volume continued to be greater than the combined share volume of all national exchanges, other than the New York Stock Exchange.

Quotations for 2,575 securities were in the System at the end of 1977, compared with 2,627 at the end of 1976. Market makers had 19,479 positions, for an average of 7.6 per security, compared with 16,960 positions and an average of 6.5 per security. The number of market makers was 353 at year's end, and 367 at the end of 1976.

The NASDAQ Composite Index, the market-value weighted index for some 2,350 domestic common securities in the System, in July went over the 100 mark for the first time since November 1973. It stayed above 100 almost continually thereafter and closed at 105.05, up 7.3% from the beginning of the year. Among the other NASDAQ indexes, the Utility Index posted a 16.2% gain, the Industrial 9.3%, the Insurance 8.8%, the Other Finance 3.9% and the Bank Index a gain of 2.8% during 1977. The Transportation Index fell 3.6%.

Market Surveillance

The NASD Market Surveillance Section in 1977 conducted 734 special reviews of unusual price and volume activity in the NASDAQ/OTC Market, signalled by the computer-generated, overnight Stock Watch Report. As a result of these reviews, 60 detailed investigations were pursued and 13 cases were referred to the District Offices and to the SEC for further investigation and for disciplinary action, where appropriate.

Early in 1978, the overnight Stock Watch Report will be supplemented by an on-line report which will immediately upon occurrence advise the Market Surveillance Section of unusual changes in market maker quotations. In addition to shortening the response time of Market Surveillance to situations requiring review, the on-line report will also enable the Section to identify more quickly instances in which quotations halts would be appropriate, so that companies might release and the investing public might digest significant news concerning the companies.

Governmental Recognition of NASDAQ Securities

FRB Margin List Additions

One hundred and ninety-five NASDAQ stocks were added to the Federal Reserve Board's re-

vised OTC Margin List of August 15, 1977. The total list included 1,106 securities, close to half of all the domestic common securities quoted on the NASDAQ System. The net gain over the December 30, 1976 list was 139 stocks, with 56 deleted because they no longer met the FRB's margin criteria, were listed on a stock exchange or because their issuers were acquired by other companies.

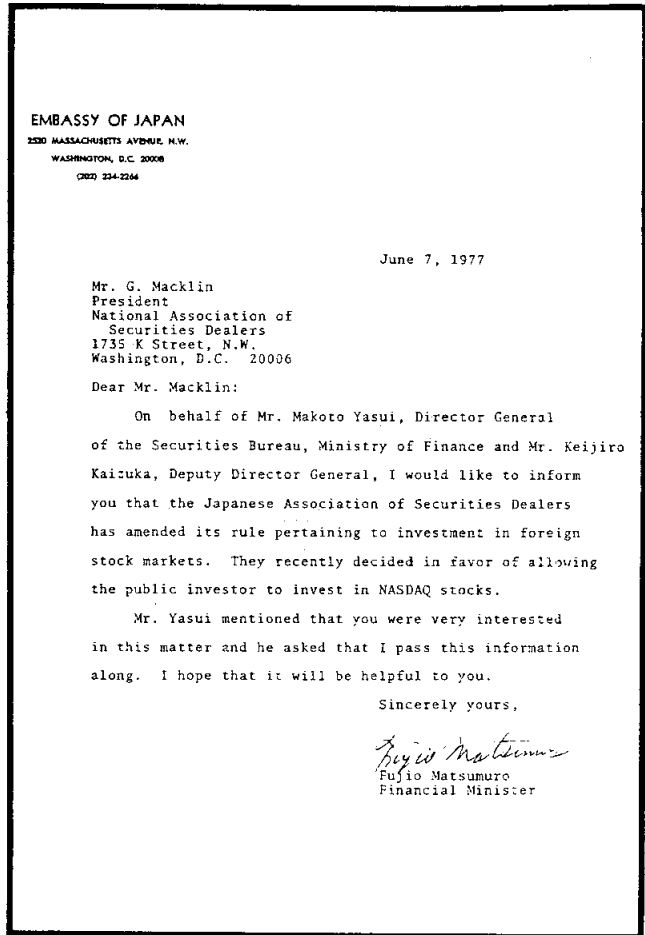
"Blue Chip" Exemptions in the States

The North American Securities Administrators Association in October approved a proposal for an extended "Blue Chip" exemption from state registration requirements in connection with distributions of securities. The proposal basically puts NASDAQ issues on a par with listed issues in qualifying for the exemption, although its requirements with respect to earnings and defaults of issuers are somewhat more stringent for NASDAQ issues than for NYSE and AMEX listed securities.

Some of the states can adopt the proposal by administrative ruling, while others must amend their statutes. The Association will communicate with the states on implementing the "Blue Chip" exemption for NASDAQ securities.

NASDAQ Securities in Japan

Increased recognition abroad has also been granted to NASDAQ securities. Through decisions of the Japanese Association of Securities Dealers and the Ministry of Finance of Japan, NASDAQ securities were on June 1, 1977 declared eligible for purchase by Japanese investors.

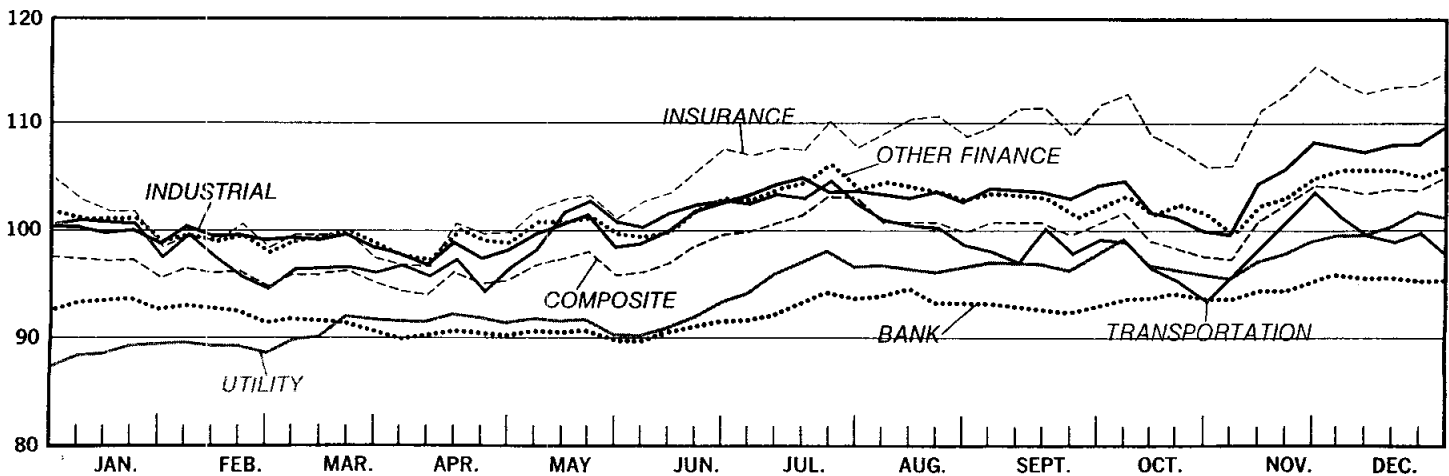


Letter from Japanese Embassy in Washington announces approval of NASDAQ securities for investment by Japanese.

NASDAQ STOCK PRICE INDEXES
(WEEKLY CLOSING VALUES)

1977

INDEX: February 5, 1971 = 100



Media Coverage of the NASDAQ/OTC Market

Press Coverage

National and regional newspapers across the country—Chicago, Columbus (Ohio), Dallas, Dayton, Los Angeles, Milwaukee, Minneapolis, New York, Providence, San Francisco, etc.—reported extensively on the good volume and price performance of the NASDAQ/OTC Market and on its growing significance.

The *Dallas Times Herald* became the 54th newspaper carrying the National NASDAQ/OTC list of the 1,410 issues which rank highest by dollar volumes of shares traded.

Over 300 other newspapers carried shorter lists of NASDAQ securities.

Radio Coverage

The UPI Audio service, with 900 client radio stations, joined other wire services and national and regional radio networks in transmitting NASDAQ market statistics. The total number of radio stations including NASDAQ data grew from an estimated 1,500 at the beginning of 1977 to an estimated 2,000 at year's end. There were particularly good gains of stations confirmed as broadcasting NASDAQ statistics in Arizona, California, Florida, Kentucky, Ohio and Virginia.

TV Coverage

TV coverage of NASDAQ continued on over 200 stations affiliated with the Public Broadcasting Service (through the weekend *Wall Street Week* show) and on some 160 cable TV stations. A dozen commercial TV stations added NASDAQ information to their reports, bringing the total of such stations to the vicinity of 50.

Communications with NASDAQ Companies

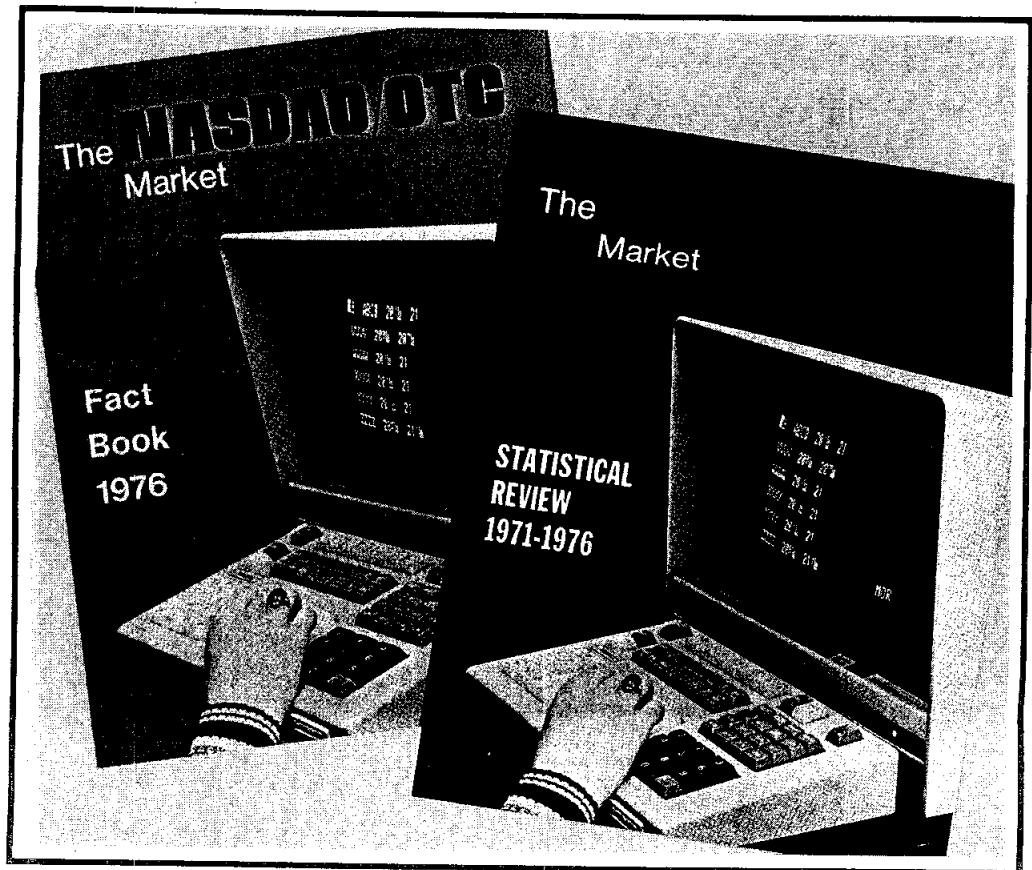
NASDAQ Fact Book

The NASDAQ/OTC Market Fact Book 1976 was published in February 1977. It contained definitive data on shareowners, volume, market value, market makers, marginable securities, most active stocks and on the performance of all securities in the market. The *Fact Book*, the first of its kind, was distributed to all NASDAQ companies, NASD members and branches, government officials and others. It helped to increase the visibility and the understanding of the NASDAQ/OTC Market, and was particularly useful in increasing media coverage of the market.

Statistical Review 1971-1976

As a sequel to the *Fact Book*, a *Statistical Review 1971-1976* of the NASDAQ/OTC Market was

Fact Book and Statistical Review had print-runs of 17,000 copies each.



published in July. The *Statistical Review* charted indexes, volume, securities and market makers throughout the existence of the NASDAQ System, and made the history of the market as visible as the *Fact Book* had made 1976.

Seminars for NASDAQ Companies

Day-long NASD Seminars for NASDAQ Companies were held in Chicago in September and in New York in October, with a combined attendance of 130 NASDAQ company executives. Topics covered included the emerging National Market System, developments in the OTC market, market making, surveillance, capital raising in the current environment and the pros and cons of being on NASDAQ. SEC Commissioner John R. Evans was the luncheon speaker.

Independent Audit Committee Survey

The SEC asked the NASD to consider whether the establishment of an Independent Audit Committee by a company should constitute a requirement for quotation on NASDAQ. The Association surveyed all NASDAQ companies as to their practices and views on the matter. The survey results will be an important factor in the NASD Board's consideration of the issue in 1978.

The NASDAQ System

Savings to Subscribers

A refund of \$1,000,000—reflecting an 8% reduction in NASDAQ rates—was distributed among subscribers in late 1977, on the basis of their billings during the preceding fiscal year. The refund was a result of NASD acquisition of the NASDAQ System in 1976.

Statistics and Performance

The number of NASDAQ Level 2 and Level 3 terminals used by subscribers increased from 1,061 to 1,099 during the year. The number of desk-top terminals showing Level 1 representative quotations for NASDAQ securities increased from 31,750 to 34,680.

The reliability of the NASDAQ System continued to be excellent. Downtime at the Central Processing Complex was less than 1/10th of 1% of total operating time. Average annual downtime per terminal due to equipment failure was approximately 34 minutes. The System processed an average of 756,185 calls per day with an average response time of less than three seconds. Peak traffic from Level 2 and Level 3 terminals located in trading rooms reached 932,242 calls.

Major Upgrading of System Equipment

In 1977, the Board of Directors of NASDAQ, Inc. approved the replacement of the existing UNIVAC 1108 computers with two UNIVAC 1100/22s. The new processors provide 512,000 words of memory, or double the capacity of the 1108s. The expanded memory will in 1978 permit the addition of further new services to the System, and a more efficient utilization of total System facilities.

The NASDAQ, Inc. Board also approved the move of the Central Processing Complex into new leased space in the Trumbull (Connecticut) Industrial Park, a very short distance away from space owned by the Bunker Ramo Corporation, the System operator. The new space has the advantage of being exclusively devoted to NASDAQ use.

New System Services

Non-NASDAQ Terminal Interface

Work was completed in 1977 on an interface which will in 1978 permit market data distributors and interested NASD member firms to use their own terminal equipment for services hitherto available only on NASDAQ Level 2 and Level 3 terminals. If the interface is utilized, subscribers will receive a reduction in their NASDAQ rates of \$75/month for the first terminal and \$15/month for each additional terminal at the same location.

NASDAQ/AutEx Interface

Toward the end of the year, NASDAQ subscribers were surveyed to determine if sufficient interest existed in an interface which would permit them to use their Level 3 terminals to enter Block Interest messages for distribution through the AutEx network. If the interface is implemented, NASDAQ subscribers to this service would have capabilities similar to those available on AutEx terminals at a lower overall cost than the lowest AutEx service rate.

Adaptation of NASDAQ to a National Market System

CQS

The Consolidated Quotations Service (CQS), the second major step after the Consolidated Tape toward a National Market System trading facility, became operational in January 1977. CQS shows quotations on all New York Stock Exchange listed securities from the Midwest, New York, Pacific and Philadelphia Stock Exchanges and from participating Third Market makers. At start-up CQS was received by subscribers on 129 terminals, and on 160 terminals at the end of the year.

For implementation in 1978, the Board of Directors of NASDAQ, Inc. directed that there be added to CQS:

- Quotations on the American and regional stock exchange listed securities on CTA Tape B;
- Last sale information for CTA Tape A and Tape B securities; and
- Display of size for CQS securities, if proposed SEC Rule 11Ac1-1 becomes effective.

These additions will make NASDAQ terminals with CQS a source of comprehensive information on some 5,300 securities, 2,600 OTC and 2,700 listed.

TMTR

NASDAQ's Third Market Transaction Reporting System in 1977 processed reports of 188,000 OTC transactions in listed securities by 259 NASD members, with an aggregate volume of 251 million shares of stocks whose primary markets are on the New York and American Stock Exchanges.

Planning for the NMS Trading Facility

In his October 10 letter to SEC Chairman Williams, offering NASD help on the development of a National Market System (NMS), NASD Chairman Arnold recommended "development of a plan . . . to coordinate and possibly construct the necessary

industry facilities" for the System. While the Association awaited a reply from the SEC, its Automation Committee began work on such a plan.

The Committee tentatively defined the essential components of an NMS trading facility as follows:

1. A Composite Quotations System (CQS) which would gather firm quotes with size from all markets and provide a visual display as well as a computerized data base of all quotes in a given security;

2. A National Order Routing (NOR) System that would include a switch connecting all markets to all broker/dealer order entry systems and would include the capability to route broker-addressed orders as well as determine the routing of unaddressed orders on the basis of CQS information;

3. A Composite Limit Order Book (CLOB) which could be added on to the order routing system to provide a central repository for the storage and execution of all limit orders. This might be a so-called "soft" CLOB—a repository allowing broker/dealer entry but only specialist and market maker execution—or a "hard" CLOB—a repository allowing broker/dealer entry and execution.

At the end of the year, the Automation Committee was engaged in an examination of how the NASDAQ System and other industry computer capabilities and communications networks might be adapted and coordinated to serve the projected NMS trading facility.



NASDAQ company executives participate in Chicago seminar presented by NASD.

Government Relations and Legal Activities

Legislation

Amendments to Securities Investor Protection Act of 1970

On November 1, 1977, the House of Representatives adopted a bill to amend the Securities Investor Protection Act of 1970. Senate passage of the bill is expected in early 1978. In past testimony before Congress, the NASD had generally supported the bill, which provides for expedited procedures for handling SIPC trusteeships and increases the overall coverage afforded to investors who deal with SIPC members.

The House struck out provisions the Association had opposed, which would have assessed income from the sales of mutual funds and variable contracts and would have required broker/dealers distributing only these products to become members of SIPC. However, the House version of the bill does contain other provisions against which the Association had testified. These provisions include gross profits from money market instruments in the base for computing SIPC assessments and require the display of the SIPC symbol in certain advertising.

Study of Other Legislative Developments

The NASD Office of General Counsel continued to follow other legislative developments of particular interest to the Association and its members. These included three bills introduced by Senator Harrison A. Williams, Jr.: (1) a bill concerning the securities activities of commercial banks and resulting from the SEC study of the subject; (2) a bill requiring municipal securities disclosure; and (3) a bill increasing the ceiling on public offerings which can be registered under Regulation A, which simplifies procedures for small issues.

Litigation

In the arbitration proceeding entitled *Bunker Ramo v. NASD*, it had been alleged that the NASD was obligated to purchase certain parts from Bunker Ramo. The proceeding was satisfactorily concluded in 1977.

During the year, the Association successfully defended against a number of actions which

sought to enjoin its disciplinary proceedings.

There were a number of cases pending against the Association at the end of 1977. These included *Quinonez v. Merrill Lynch, et al.* and *Baty v. Pressman, Frohlich & Frost, et al.*, which had been pending a year earlier. The Office of General Counsel believes that meritorious defenses are available in all these matters.

NASDAQ, Inc. filed an application in 1976 with the Internal Revenue Service for exemption from federal income taxes. In a letter dated February 9, 1978, the IRS ruled that the Corporation does not qualify for exemption. This ruling is being protested, because management feels that NASDAQ, Inc. operations represent tax-exempt activities.

National Clearing Corporation

The foundation for a single national clearance and settlement system—a major component of the projected National Market System—was laid in 1977 with the consolidation of the Association's National Clearing Corporation (NCC) with the clearing corporations of the American and New York Stock Exchanges into the new National Securities Clearing Corporation (NSCC).

The first phase of the consolidation, as approved by the SEC, consisted of an organizational merger of the three entities, under a Board of Directors with 12 user representatives and 4 other members. In this phase, the NASD transferred the assets and liabilities of NCC to NSCC, in return for a one-third ownership of NSCC and a note for \$600,000, which was paid to the Association in September.

During the year, NSCC provided clearing services through two systems, one for OTC and the other for listed securities, and worked toward the second phase of the merger, in which there is to be a single system for clearing both OTC and listed securities. The SEC laid down four conditions for the single system: (1) NSCC to establish interfaces with various clearing corporations and depositories; (2) NSCC to develop a method whereby broker/dealers who do not maintain offices in New York City may either directly or through an agency compare their transactions with

NSCC members; (3) NSCC to make available the regional branches inherited from NCC to participants in other clearing agencies, if they should so desire; (4) NSCC to furnish its computer programs for OTC trade comparison to other clearing agencies at no charge, and to arrange for an agency other than NSCC to compare transactions between participants in different clearing agencies, or else to perform this service at no charge.

At the end of 1977, NSCC had not been able fully to meet all these conditions, particularly the

completion of interfaces with the clearing corporations of the regional exchanges. Bradford National Clearing Corporation, the facilities manager for the NCC division of NSCC, filed legal challenges to the consolidation and its implementation, and declined to make certain system changes requested by NSCC. At the end of the year, NSCC pursued its efforts to reach an understanding with Bradford and also prepared alternative plans for proceeding toward the single clearing system.

THE AGENDA FOR '78

As this Report to Members 1977 has indicated, the NASD has many tasks in many areas before it in 1978. These include:

- **Membership communications**—to issue better written materials, develop more useful discussion meetings on industry issues and encourage more membership contributions to Association policy formulation;

- **Membership services**—to make work the "one-window" system for administrative assistance to member firms, in which each firm will have a single point of contact in the Registration Section;

- **Examinations and surveillance**—to decrease the number of violations through further educational programs, to reduce regulatory burdens through still more efficient examination procedures, and to reduce the industry's duplication

of effort by additional coordination with other self-regulatory organizations;

- **Regulatory policy**—to work with the SEC on resolving the problems in securities distribution practices, to work with other organizations for a uniform industry-wide arbitration system, to promote compliance in direct participation program offerings, and to try to eliminate the obstacles to a NASDAQ options program;

- **The NASDAQ/OTC market**—to increase recognition of the market, improve communications with present and potential NASDAQ issuers, and expand the services of the NASDAQ System;

- **Clearing**—to support the progress of the National Securities Clearing Corporation toward a single system for OTC and listed securities; and

- **The National Market System**—to cooperate with other industry organizations in the development of a trading facility and a regulatory structure.

1977 NASD APPEARANCES AND SUBMISSIONS

During 1977, the Association made four appearances before the SEC (in addition to many informal conferences with Commissioners and staff) and submitted 27 letters of comment or reports to the SEC and other governmental branches. The issues addressed are given in alphabetical order, and the appearances and comments on them are summarized in chronological order.

Confirmation Rule (Rule 10b-10)

September 7 letter to the SEC, particularly opposing proposed requirements to disclose the "inside market" and mark-ups and mark-downs on riskless principal transactions. (See also Investment Company Regulation, below).

FOCUS Reporting System

March 2 letter to the SEC, concurring with all proposed amendments except that of Rule 17a-19, which would impose a rather substantial reporting burden on the Association.

Investment Company Regulation

August 3 letter to the SEC, expressing reservations about proposed Rule 434d relating to investment company advertising.

September 7 letter to the SEC (see above), also criticizing its proposal to amend the Confirmation Rule with regard to quarterly confirmations for investment company plans.

October 31 letter to the SEC, commenting on certain revisions of the SEC's Statement of Policy regarding investment company advertising.

December 14 letter to the SEC, commenting on the Commission's proposed general reexamination of the Statement of Policy.

Investors' Small Claims Resolution

January 28 letter to the SEC, advocating a securities industry task force to develop an investors' small claims resolution system.

February 10 appearance before the SEC, to develop views expressed in the January 28 letter.

December 8 appearance before the SEC, on behalf of the Securities Industry Conference on Arbitration proposals.

Municipal Securities Regulation

February 17 letter to the SEC, expressing concern at the impact on the municipal securities industry of the inquiry requirements of Rule 17f-1 regarding lost and stolen securities.

February 18 letter to the SEC, concerning the MSRB's proposed Rule G-12 on Uniform Practice.

March 2 letter to the SEC, commenting on proposed amendments to the Uniform Net Capital Rule pertaining to transactions in municipal securities.

April 20 letter to the MSRB, commenting on its proposed Rules G-11A and G-11B on underwriting practices and the sale of new issues of municipal securities.

April 21 letter to the SEC, expanding on the February 17 letter (above) regarding Rule 17f-1.

June 3 letter to the SEC, expanding on the March 2 letter (above).

September 7 letter to the House Subcommittee on Oversight and Investigation and the Subcommittee on Consumer Protection and Finance, outlining the NASD's actions in carrying out its responsibilities for municipal securities regulation under the Securities Acts Amendments of 1975.

November 23 letter to the SEC, regarding the MSRB's proposed Rule G-16 on periodic compliance examinations of municipal securities firms and recommending a minimum of one examination a year.

December 16 letter to the MSRB, recommending a modification of its proposed Rule G-34 on advertising.

National Market System

June 21 appearance before the SEC, with comments on the functioning and administration of a National Market System.

October 10 letter from NASD Chairman Eugene Arnold, Jr. to SEC Chairman Harold M. Williams, concerning the Association's readiness to play a coordinating role in National Market System development.

Off-Board Trading Restrictions

August 16 appearance before the SEC, with recommendation that no new rules in the over-the-

counter market would be needed if off-board trading restrictions were removed.

September 14 submission to the SEC of a *Summary of the National Association of Securities Dealers, Inc.'s Current Surveillance Programs and Planned Enhancements Thereto as Such Relate to Matters Under Consideration by the Commission in Connection with Its Proposal to Remove Off-Board Trading Restrictions.*

September 19 letter to the SEC, refuting criticism by the New York Stock Exchange of the NASD's testimony before the Commission on August 16.

Options on NASDAQ

January 10 letter to the SEC, concerning proposed amendments to the Uniform Net Capital Rule as they affect certain options market makers and broker/dealers.

January 14 submission to the SEC of the proposed rules to govern the NASDAQ Options Program.

March 18 letter to the SEC, declaring inappropriate public dissemination, on a real-time basis, of last sale information on OTC securities which underlie exchange-traded options.

June 3 letter to the Board of Governors of the Federal Reserve System, suggesting that, with respect to margin requirements for transactions in options, NASDAQ market makers in both options and equities receive the same treatment as exchange specialists.

August 26 letter to the SEC, protesting the SEC options moratorium and the suspension of the NASDAQ options program.

September 21 letter to the SEC, supporting proposed rules of the Options Clearing Corporation which would facilitate the NASD's becoming a participant owner of the OGC.

December 9 letter to the SEC, taking exception to the Commission's contemplated disapproval proceedings of the proposed NASDAQ options program.

December 12 letter to the SEC, expressing concern about the legality and the effect of SEC investigative proceedings on the proposed NASDAQ options program.

Qualification

August 10 letter to the SEC, detailing the differences between the SEC's qualification requirements for brokers, dealers and associated persons and the NASD's recommendations on such requirements.

Service Bureaus

May 6 letter to the SEC, registering substantial agreement and suggesting some changes to proposed amendments to Rule 17a-4 concerning the filing of agreements by outside service bureaus.

Short Selling

March 18 letter to the SEC, objecting to its currently proposed version of Rule 10b-21 on short selling, and supporting the April 1975 version of the proposed rule.

May 27 letter to the SEC, recommending that market makers be excluded from the provisions of proposed Rule 10b-11.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Governors of National Association of Securities Dealers, Inc. and NASDAQ, Inc.

We have examined the accompanying individual and consolidated balance sheets of the National Association of Securities Dealers, Inc. (NASD) and its subsidiary NASDAQ, Inc. as of September 30, 1977 and 1976, and the related statements of operations and Association equity and of changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As further described in Note 2, NASDAQ, Inc. has applied for exemptions from Federal and state income taxes and has not provided for these taxes in the accompanying financial statements.

As further described in Note 10, NASD is a defendant in several legal actions, the outcome of which is not presently determinable.

In our opinion, subject to the effect of such adjustments, if any, as might have been required had the outcome of the matters referred to in the two preceding paragraphs been known, the financial statements examined by us present fairly the individual and consolidated financial position of the National Association of Securities Dealers, Inc. and NASDAQ, Inc. at September 30, 1977 and 1976, and the individual and consolidated results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied.

Washington, D.C.
January 11, 1978

PRICE WATERHOUSE & CO.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
AND NASDAQ, INC.

BALANCE SHEETS

September 30,

| | 1977 | | | 1976 | | |
|---|----------------------------------|---------------------|---------------------|----------------------------------|---------------------|---------------------|
| | NASD (Parent Organization) | NASDAQ | Consolidated | NASD (Parent Organization) | NASDAQ | Consolidated |
| Assets | | | | | | |
| Current assets | | | | | | |
| Cash | \$ 150,737 | \$ 163,541 | \$ 314,278 | \$ 133,747 | \$ 104,098 | \$ 237,845 |
| Investment securities, at cost (approximate market value for 1977: NASD \$6,088,000 NASDAQ \$6,251,000; for 1976: NASD \$4,037,000, NASDAQ \$3,409,000.) | 6,132,726 | 6,298,345 | 12,431,071 | 4,000,075 | 3,409,987 | 7,410,062 |
| Other current assets | 731,400 | 879,415 | 1,505,646 | 664,087 | 696,340 | 1,272,836 |
| Total current assets | 7,014,863 | 7,341,301 | 14,250,995 | 4,797,909 | 4,210,425 | 8,920,743 |
| Data processing, subscriber equipment and software, at cost less accumulated depreciation and amortization of \$5,567,787 and \$2,649,582 (Note 5) | | 4,078,110 | 4,078,110 | | 6,849,372 | 6,849,372 |
| Investments in | | | | | | |
| Wholly-owned subsidiaries, at equity in net assets (Notes 1 and 2) | | | | | | |
| National Clearing Corporation (Note 7) | 902,894 | | 902,894 | 1,458,779 | | 1,458,779 |
| NASDAQ, Inc. | 1,802,535 | | | 402,299 | | |
| Investment securities, at cost (approximate market value of \$4,557,000 and \$4,605,000) (Note 5) | 4,497,802 | | 4,497,802 | 4,492,464 | | 4,492,464 |
| Depository Trust Company, at cost (Note 8) | 215,585 | | 215,585 | 258,889 | | 258,889 |
| Land, building and improvements, at cost less accumulated depreciation of \$459,955 and \$387,944 (Note 4) | 3,005,440 | | 3,005,440 | 3,060,819 | | 3,060,819 |
| Special investment account, at lower of cost or market (Note 2) | 251,185 | | 251,185 | 236,233 | | 236,233 |
| Other assets | 188,687 | 30,288 | 218,975 | 164,018 | 19,224 | 183,242 |
| | <u>\$17,878,991</u> | <u>\$11,449,699</u> | <u>\$27,420,986</u> | <u>\$14,871,410</u> | <u>\$11,079,021</u> | <u>\$25,460,541</u> |
| Liabilities and Association Equity | | | | | | |
| Current liabilities | | | | | | |
| Accounts payable and accrued expenses | \$ 829,954 | \$ 647,164 | \$ 1,371,949 | \$ 813,323 | \$ 676,722 | \$ 1,402,454 |
| Prepaid NASDAQ issuers fees | 1,569,431 | | 1,569,431 | 1,546,418 | | 1,546,418 |
| Current portion of mortgage payable | 105,316 | | 105,316 | 99,693 | | 99,693 |
| Current portion of notes payable (Note 5) | | 2,000,000 | 2,000,000 | | 2,000,000 | 2,000,000 |
| Refund of user services fees (Note 2) | | 1,000,000 | 1,000,000 | | | |
| | 2,504,701 | 3,647,164 | 6,046,696 | 2,459,434 | 2,676,722 | 5,048,565 |
| Long-term liabilities | | | | | | |
| Reserve for deferred compensation | 251,185 | | 251,185 | 236,233 | | 236,233 |
| Mortgage payable (Note 4) | 935,023 | | 935,023 | 1,040,339 | | 1,040,339 |
| Note payable (Note 5) | | 6,000,000 | 6,000,000 | | 8,000,000 | 8,000,000 |
| Total liabilities | 3,690,909 | 9,647,164 | 13,232,904 | 3,736,006 | 10,676,722 | 14,325,137 |
| Association equity (Note 5) | 14,188,082 | 1,802,535 | 14,188,082 | 11,135,404 | 402,299 | 11,135,404 |
| Commitments and contingencies (Notes 5, 9 and 10) | | | | | | |
| | <u>\$17,878,991</u> | <u>\$11,449,699</u> | <u>\$27,420,986</u> | <u>\$14,871,410</u> | <u>\$11,079,021</u> | <u>\$25,460,541</u> |

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
AND NASDAQ, INC.

STATEMENTS OF OPERATIONS AND ASSOCIATION EQUITY

| | Year Ended September 30, | | | | | |
|---|----------------------------------|---------------------|---------------------|----------------------------------|--------------------|---------------------|
| | 1977 | | | 1976 | | |
| | NASD (Parent Organization) | NASDAQ (Note 2) | Consolidated | NASD (Parent Organization) | NASDAQ (Note 2) | Consolidated |
| Income | | | | | | |
| Member assessments and branch office fees | \$ 7,317,460 | | \$ 7,317,460 | \$ 6,511,681 | | \$ 6,511,681 |
| NASDAQ user services fees | | \$12,921,312 | 12,921,312 | | \$7,966,112 | 7,966,112 |
| Registered representative fees | | | | | | |
| Applications | 1,316,410 | | 1,316,410 | 1,340,370 | | 1,340,370 |
| Examinations | 1,158,468 | | 1,158,468 | 1,063,256 | | 1,063,256 |
| Corporate finance fees | 909,126 | | 909,126 | 1,049,541 | | 1,049,541 |
| Fines | 212,300 | | 212,300 | 219,097 | | 219,097 |
| Interest and other income | 907,447 | 289,653 | 1,197,100 | 777,139 | 46,822 | 823,961 |
| NASDAQ issuers fees | 2,716,621 | | 2,716,621 | 2,642,122 | | 2,642,122 |
| Regulatory service for NCC/NSCC (Note 3) | 1,167,907 | | 1,167,907 | 619,070 | | 619,070 |
| Refund of user services fees (Note 2) | | (1,000,000) | (1,000,000) | | | |
| | <u>15,705,739</u> | <u>12,210,965</u> | <u>27,916,704</u> | <u>14,222,276</u> | <u>8,012,934</u> | <u>22,235,210</u> |
| Expenses | | | | | | |
| Salaries and employee benefits | 9,252,545 | 926,076 | 10,178,621 | 8,986,876 | 414,594 | 9,401,470 |
| Travel, meeting and investigation expenses | 1,205,984 | 118,258 | 1,324,242 | 1,027,943 | 60,021 | 1,087,964 |
| Publication, stationery and postage (net of publication sales of \$40,749 in 1977 and \$39,562 in 1976) | 736,234 | 109,890 | 846,124 | 687,695 | 10,426 | 698,121 |
| Professional and other services | 677,430 | 111,671 | 789,101 | 607,945 | 110,431 | 718,376 |
| Occupancy expenses | 944,666 | 136,304 | 1,080,970 | 921,613 | 58,104 | 979,717 |
| Office, insurance and miscellaneous | 486,496 | 34,108 | 520,604 | 439,323 | 109,730 | 549,053 |
| Furniture and equipment | 61,832 | | 61,832 | 48,591 | | 48,591 |
| Interest | 60,214 | 910,000 | 970,214 | 65,537 | 676,667 | 742,204 |
| System operator's fees | | 4,031,468 | 4,031,468 | | 2,511,807 | 2,511,807 |
| Depreciation and amortization | 72,011 | 2,918,205 | 2,990,216 | 70,432 | 2,649,582 | 2,720,014 |
| Development expenses | | 524,170 | 524,170 | | 299,772 | 299,772 |
| Other operating expenses | | 990,579 | 990,579 | | 710,501 | 710,501 |
| | <u>13,497,412</u> | <u>10,810,729</u> | <u>24,308,141</u> | <u>12,855,955</u> | <u>7,611,635</u> | <u>20,467,590</u> |
| Net income (deficit) | | | | | | |
| NASD | 2,208,327 | | 2,208,327 | 1,366,321 | | 1,366,321 |
| NCC (Note 7) | (555,885) | | (555,885) | 205,800 | | 205,800 |
| NASDAQ, Inc. | 1,400,236 | 1,400,236 | 1,400,236 | 401,299 | 401,299 | 401,299 |
| Consolidated | <u>3,052,678</u> | | <u>3,052,678</u> | <u>1,973,420</u> | | <u>1,973,420</u> |
| Association equity, beginning of year | 11,135,404 | 402,299 | 11,135,404 | 9,161,984 | | 9,161,984 |
| Issuance of common stock (Note 1) | | | | | 1,000 | |
| Association equity, end of year | <u>\$14,188,082</u> | <u>\$ 1,802,535</u> | <u>\$14,188,082</u> | <u>\$11,135,404</u> | <u>\$ 402,299</u> | <u>\$11,135,404</u> |

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
AND NASDAQ, INC.

STATEMENTS OF CHANGES IN FINANCIAL POSITION

| | Year Ended September 30, | | | | | |
|--|----------------------------------|---------------------|---------------------|----------------------------------|---------------------|----------------------|
| | 1977 | | | 1976 | | |
| | NASD (Parent Organization) | NASDAQ (Note 2) | Consolidated | NASD (Parent Organization) | NASDAQ (Note 2) | Consolidated |
| Financial resources were provided by | | | | | | |
| Net income | \$ 2,208,327 | \$ 1,400,236 | | \$ 1,366,321 | \$ 401,299 | |
| Net income (loss) of NCC | (555,885) | | | 205,800 | | |
| Net income of NASDAQ, Inc. | 1,400,236 | | | 401,299 | | |
| | <u>3,052,678</u> | <u>1,400,236</u> | <u>3,052,678</u> | <u>1,973,420</u> | <u>401,299</u> | <u>1,973,420</u> |
| Items not affecting working capital in the period: | | | | | | |
| Net income of wholly-owned subsidiaries | (844,351) | | 555,885 | (607,099) | | (205,800) |
| Depreciation and amortization | 72,011 | 2,918,205 | 2,990,216 | 70,432 | 2,649,582 | 2,720,014 |
| Issuance of note payable | | | | | 10,000,000 | 10,000,000 |
| Issuance of common stock | | | | | 1,000 | |
| | <u>2,280,338</u> | <u>4,318,441</u> | <u>6,598,779</u> | <u>1,436,753</u> | <u>13,051,881</u> | <u>14,487,634</u> |
| Financial resources were used for | | | | | | |
| Purchase of data processing, subscriber equipment and software | | 146,943 | 146,943 | | 9,498,954 | 9,498,954 |
| Investment in subsidiary | | | | 1,000 | | |
| Increase in non-current investment securities | 5,338 | | 5,338 | 4,492,464 | | 4,492,464 |
| Increase (decrease) in investment in Depository Trust Company | (43,304) | | (43,304) | 258,889 | | 258,889 |
| Purchase of building improvements | 16,632 | | 16,632 | 14,956 | | 14,956 |
| Increase in other assets | 24,669 | 11,064 | 35,733 | 7,143 | 19,224 | 26,367 |
| Decrease in long-term note payable | | 2,000,000 | 2,000,000 | | 2,000,000 | 2,000,000 |
| Decrease in long-term mortgage payable | 105,316 | | 105,316 | 99,693 | | 99,693 |
| | <u>108,651</u> | <u>2,158,007</u> | <u>2,266,658</u> | <u>4,874,145</u> | <u>11,518,178</u> | <u>16,391,323</u> |
| (Decrease) increase in working capital | <u>\$ 2,171,687</u> | <u>\$ 2,160,434</u> | <u>\$ 4,332,121</u> | <u>\$(3,437,392)</u> | <u>\$ 1,533,703</u> | <u>\$(1,903,689)</u> |
| Analysis of Changes in Working Capital | | | | | | |
| Increase (decrease) in current assets | | | | | | |
| Cash | \$ 16,990 | \$ 59,443 | \$ 76,433 | \$ (3,718) | \$ 104,098 | \$ 100,380 |
| Investment securities | 2,132,651 | 2,888,358 | 5,021,009 | (3,622,552) | 3,409,987 | (212,565) |
| Other current assets | 67,313 | 183,075 | 232,810 | 276,471 | 696,340 | 885,220 |
| | <u>2,216,954</u> | <u>3,130,876</u> | <u>5,330,252</u> | <u>(3,349,799)</u> | <u>4,210,425</u> | <u>773,035</u> |
| Decrease (increase) in current liabilities | | | | | | |
| Accounts payable and accrued expenses | (16,631) | 29,558 | 30,505 | (934) | (676,722) | (590,065) |
| Prepaid NASDAQ issuers fees and assessments | (23,013) | | (23,013) | (81,335) | | (81,335) |
| Current portion of mortgage payable | (5,623) | | (5,623) | (5,324) | | (5,324) |
| Current portion of notes payable | | | | | (2,000,000) | (2,000,000) |
| Refund of user services fees | | (1,000,000) | (1,000,000) | | | |
| | <u>(45,267)</u> | <u>(970,442)</u> | <u>(998,131)</u> | <u>(87,593)</u> | <u>(2,676,722)</u> | <u>(2,676,724)</u> |
| Increase (decrease) in working capital | <u>\$ 2,171,687</u> | <u>\$ 2,160,434</u> | <u>\$ 4,332,121</u> | <u>\$(3,437,392)</u> | <u>\$ 1,533,703</u> | <u>\$(1,903,689)</u> |

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. AND NASDAQ, INC.

NOTES TO FINANCIAL STATEMENTS

Note 1—Organization

The National Association of Securities Dealers, Inc. (NASD) is a not-for-profit membership association established to regulate the over-the-counter securities market. The NASD owns 100% of the common stock of National Clearing Corporation (NCC) (Note 7) and on January 29, 1976, acquired 1,000 shares of NASDAQ, Inc.'s \$1 par value common stock which is the total number of shares authorized, issued and outstanding. NASDAQ, Inc. was established to acquire and operate the NASDAQ system.

Note 2—Summary of Significant Accounting Policies Investment in NCC and NASDAQ, Inc.

The NASD's investment in NCC is recorded at its equity in net assets and accordingly is adjusted for the net income or loss of NCC. Summary financial information for NCC is presented in Note 7.

The consolidated financial statements include the accounts of the NASD and NASDAQ, Inc. after elimination of all significant intercompany transactions. The operations of NASDAQ, Inc. are included in the accompanying financial statements from February 9, 1976, the date it acquired the assets of the NASDAQ system; thus, the financial statements include only eight months of operations for NASDAQ, Inc. in 1976.

Retirement Benefits and Deferred Compensation

NASD maintains a non-contributory trustee pension plan for the benefit of all eligible employees. Certain employees have been granted extended retirement and death benefits. It is NASD's policy to fund pension costs and to provide for the cost of other benefits as they accrue. Pension and deferred compensation costs were \$347,907 and \$300,369 for the years ended September 30, 1977 and 1976, respectively.

The Special Investment Account represents amounts set aside to fund the reserve for deferred compensation which relates to five former or current employees.

Depreciation and Amortization

NASD's building and improvements are being depreciated on a straight-line basis over lives of 38 and 10 years, respectively. Purchases of office furniture and equipment by NASD are treated as an expense in the year acquired.

NASDAQ, Inc.'s data processing, subscriber equipment and software acquired on February 9, 1976 are being depreciated and amortized on an accelerated basis over 3 years. Other NASDAQ equipment, subsequently acquired, is being depreciated using various methods over useful lives of from 3 to 10 years.

Prepaid NASDAQ Issuers Fees

Prepaid NASDAQ issuers fees are deferred and included in income of the applicable fiscal year.

Income Taxes

NASD is a tax-exempt not-for-profit organization. NASDAQ, Inc. has applied for exemptions from Federal and state income taxes. If favorable tax rulings are not received, Federal and state income taxes of approximately \$950,000 will be payable for the period from inception through September 30, 1977. No provision for income taxes related to NASDAQ, Inc. has been made in the accompanying financial statements.

Refund of User Service Fees

During 1977, the governing Boards of NASDAQ, Inc. and the NASD approved a \$1,000,000 refund of NASDAQ user services fees. The refund reflects a reduction in rates for 1977.

Note 3—Related Party Transactions

NASDAQ, Inc. utilizes the services of NASD employees. In addition, NASD provides NCC/NSCC regulatory services relating to NASD members who are also members of NCC/NSCC. Such regulatory services include periodic examination of the books, records and operations of NCC/NSCC members; monitoring and investigating the financial and operating condition of members and new applications for membership; and appraising NCC/NSCC of unusual market conditions which affect securities cleared by NCC/NSCC. Of the regulatory fees paid by NCC to NASD, \$600,000 was authorized by a resolution of the Board of Directors in November 1976 for regulatory services performed prior to October 1975. In addition, NASD bills NASDAQ, Inc. and NCC/NSCC for other expenses incurred on their behalf. Billings from NASD during 1977 and 1976 for these activities are summarized as follows:

| | Billings from NASD for year ended September 30, | |
|-----------------------|--|-----------|
| | 1977 | 1976 |
| NASDAQ, Inc. | \$1,185,464 | \$663,421 |
| NCC, regulatory fees | 764,612 | 619,070 |
| NSCC, regulatory fees | 403,295 | — |
| NCC, other | 69,143 | 193,131 |

At September 30, 1977 the unpaid receivables (payables) from NASDAQ, Inc. and NCC were \$105,169 (\$87,591 in 1976) and \$9,578 (\$61,644 in 1976), respectively.

Note 4—Mortgage Payable

NASD's land and building are pledged as security for a 5½% mortgage. The mortgage loan is payable through 1985 in equal monthly instalments of principal and interest of \$13,326.

Note 5—Note Payable

All assets of the NASDAQ system are pledged as security for a 10½% note, the principal of which is payable in annual instalments of \$2,000,000 through 1981. Interest is payable quarterly and the note is guaranteed by NASD. In connection with this guarantee NASD has pledged \$4,500,000 of investment securities as collateral. Under the provision of the note agreement, NASD is required to maintain consolidated working capital of the lesser of \$4,500,000 or 125% of the outstanding principal balance of the note. The agreement provides that working capital, for purposes of the agreement, is to include the securities pledged by the NASD and is not to be reduced by the current portion of the note payable. In addition NASD is required to maintain a consolidated tangible equity of at least \$7,500,000. The note agreement contains other restrictive covenants relating to, among other things, additional indebtedness, dividends and transactions with affiliates.

Note 6—NASDAQ System

The NASDAQ quotation system commenced service on February 8, 1971, under an agreement between NASD and Bunker Ramo Corporation. NASD exercised its option to terminate the agreement and acquired the system for Bunker Ramo's undepreciated investment of \$9,498,954 on February 9, 1976, the expiration date of the original agreement. The acquisition was made through NASD's wholly-owned subsidiary, NASDAQ, Inc.

Note 7—Investment in National Clearing Corporation (NCC)

In January 1977, NCC's stock clearing operations were consolidated with those of the clearing subsidiaries of the New York Stock Exchange, Inc. and the American Stock Exchange, Inc. into the National Securities Clearing Corporation (NSCC).

Pursuant to the plan of consolidation, NCC obtained a one-third ownership interest in NSCC and a \$600,000 note (which was paid on September 15, 1977) in exchange for substantially all of its net assets of \$900,000. NSCC also assumed responsibility for NCC's leases and contracts pertaining to clearing operations.

A summary of NCC's operations and financial position for 1977 and 1976 is as follows:

| | Summary of Operations | |
|--|---------------------------------|--------------|
| | Year ended September 30 1977 | 1976 |
| Revenue, including investment income of \$35,372 and \$54,159 | \$ 2,488,778 | \$ 9,047,995 |
| Operating expenses including regulatory fee to NASD of \$764,612 and \$619,070 | 3,043,163 | 8,800,995 |
| Provision for income taxes | (554,385) | 247,000 |
| | 1,500 | 131,500 |
| Realization of tax loss carry-forward | (555,885) | 115,500 |
| Net (loss) income | (555,885) | 205,800 |
| Deficit at beginning of year | (551,221) | (757,021) |
| Deficit at end of year | \$ (1,107,106) | \$ (551,221) |

Substantially all of NCC's operating loss for the year ended September 30, 1977 relates to NCC's clearing operations for the three-month period ended December 31, 1976 which was prior to the merger of its clearing operations into NSCC.

Condensed Balance Sheets

| | September 30, | |
|---|---------------|--------------|
| | 1977 | 1976 |
| Current assets, including settlement accounts receivable of \$5,794,564 in 1976 | \$ 627,530 | \$ 7,608,762 |
| Other operating assets | | 518,141 |
| Clearing fund | | 21,491,000 |
| Investment in NSCC, at cost | 300,000 | |
| | \$ 927,530 | \$29,617,903 |
| Current liabilities including settlement accounts of \$5,438,138 in 1976 | \$ 24,636 | \$ 6,668,124 |
| Clearing fund | | 21,491,000 |
| Common stock and additional paid-in capital | 2,010,000 | 2,010,000 |
| Accumulated deficit | (1,107,106) | (551,221) |
| | 902,894 | 1,458,779 |
| | \$ 927,530 | \$29,617,903 |

The investment in NSCC is carried at cost since that corporation will be controlled by the users of the clearing facilities and does not intend to pay dividends to its shareholders.

Note 8—Investment in Depository Trust Company

Pursuant to a plan to diversify the ownership of Depository Trust Company (DTC) among various self-regulatory and other organizations, in October, 1975, NASD acquired 8% of the outstanding shares of DTC from the New York Stock Exchange. Entitlement to own shares of DTC is redetermined each year based on usage of its facilities. During 1977 and 1976 NASD sold a portion of its shares in DTC with a resulting gain (loss) of \$5,221 in 1977 and (\$811) in 1976. NASD currently owns 6.5% of the outstanding shares of DTC.

Note 9—Commitments

In connection with the operation of its district offices, NASD leases office space in various locations. Rental expense amounted to \$783,826 and \$818,308 for the years ended September 30, 1977 and 1976, respectively. Minimum lease payments for the succeeding fiscal years are as follows: \$741,217 in 1978, \$672,329 in 1979, \$416,754 in 1980, \$174,502 in 1981, \$77,416 in 1982 and \$217,429 from 1983 through 1987. No lease extends beyond 1987. The majority of these leases contain escalation clauses based on increases in property taxes and building operation costs.

NASDAQ, Inc. entered into an agreement with Bunker Ramo as of February 9, 1976. Bunker Ramo is to operate the NASDAQ system and to perform certain other services. Minimum annual payments under this agreement for the succeeding fiscal years are as follows: \$4,233,333 in 1978, \$4,433,333 in 1979 and \$1,500,000 in 1980. The agreement extends to January 31, 1980, but may be terminated by NASDAQ, Inc. upon six months notice or by either party under certain other conditions. Other NASDAQ, Inc. commitments are as follows: \$221,820 in 1978, \$431,073 in 1979, \$409,048 in 1980, \$387,021 in 1981, \$321,096 in 1982 and \$167,034 in 1983.

Note 10—Litigation

The NASD has been named, separately or with others, in several legal actions in which damages of substantial or as yet unspecified amounts are claimed. Certain of these actions allege violations of the anti-trust laws or the failure of the NASD to take appropriate action in the exercise of its regulatory responsibility. Counsel for the NASD advises that, although the NASD has meritorious defenses to all the pending litigation, the outcome of the litigation cannot be predicted.

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Section 17(f) and Related Matters

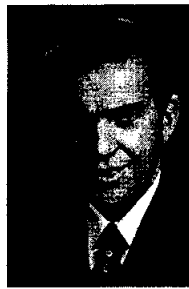
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TO SERVE UNTIL JANUARY 1978



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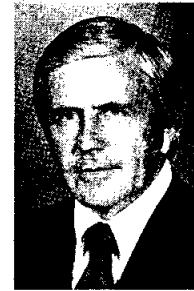
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* Governor-at-Large

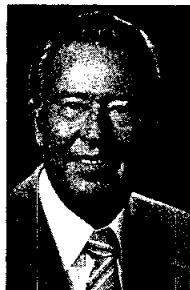
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San Francisco,
California



Raymond J. Kiernan
Merrill Lynch, Pierce,
Fenner & Smith Inc.
New York, New York



Robert A. Mackie, Jr.
Singer & Mackie, Inc.
Jersey City, New Jersey



J. Stephen Putnam
F. L. Putnam &
Company, Inc.
Boston, Massachusetts



John A. Wing
Becker Securities
incorporated
Chicago, Illinois

TO SERVE UNTIL JANUARY 1981



John D. Berl
Sutro & Co.
Incorporated
Los Angeles, California



Peter A. Bernard
Bache Halsey Stuart
Shields Incorporated
New York, New York



Douglas H. Curtis *
Franklin Electric
Co., Inc.
Bluffton, Indiana



James F. Keegan
Morgan, Keegan &
Company, Inc.
Memphis, Tennessee



John C. Printon
Printon, Kane & Co.
Summit, New Jersey



William W. Strawther, Jr.
Continental American
Securities, Inc.
Phoenix, Arizona



William Z. Suplee III
Elkins, Stroud, Suplee
& Co.
Philadelphia, Pennsylvania



David W. Wiley, Jr.
Wiley Bros., Inc.
Nashville, Tennessee

* Governor-at-Large

* Governor-at-Large

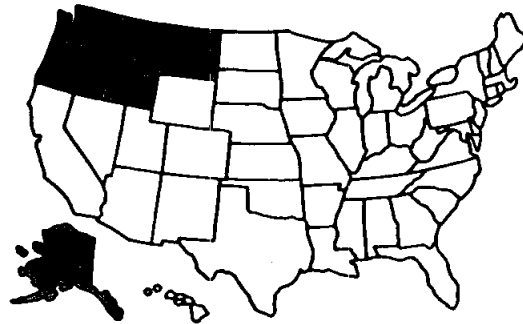
DISTRICT COMMITTEES 1977

DISTRICT NO. 1

ALASKA OREGON
 IDAHO WASHINGTON
 MONTANA



Ken Solid
 Chairman
 Smith Barney,
 Harris Upham &
 Co. Incorporated
 Seattle, Washington



David C. Grove
 Vice-Chairman
 Somers, Grove & Co., Inc.
 Portland, Oregon

Charles N. Covey
 Atkinson and Company
 Portland, Oregon

Phillip F. Frink, Jr.
 Piper, Jaffray & Hopwood
 Incorporated
 Seattle, Washington

Donald Hart
 Foster & Marshall Inc.
 Spokane, Washington

Earl McLaren
 Dean Witter & Co. Incorporated
 Seattle, Washington

E. G. Marks
 Merrill Lynch, Pierce,
 Fenner & Smith Inc.
 Spokane, Washington

Stuart C. Nicholson
 D. A. Davidson & Co.
 Great Falls, Montana

Peter D. Williams
 Blakely, Strand & Williams, Inc.
 Portland, Oregon

L. Hoyt DeMers
 Director
 1111 IBM Building
 Seattle, Washington 98101

72 MEMBERS • 274 BRANCH OFFICES • 4,899 REGISTERED REPRESENTATIVES

DISTRICT NO. 2

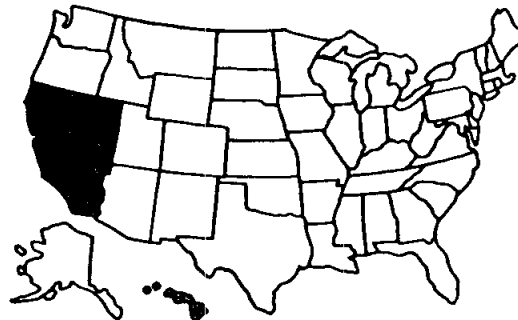
CALIFORNIA NEVADA
 HAWAII



Anthony M. Englese
 Co-Chairman
 Reynolds Securities Inc.
 San Francisco, California



John B. Callery, Jr.*
 Co-Chairman
 Newhard, Cook &
 Co., Inc.
 Los Angeles, California



James L. McPhail *
 Co-Chairman
 Morgan, Olmstead,
 Kennedy & Gardner
 Incorporated
 Los Angeles, California

William L. Bagnard
 American Funds Distributors,
 Inc.
 Los Angeles, California

William C. Bailey, Jr.
 Wagenseller & Durst, Inc.
 Los Angeles, California

Howard D. Banks
 Blyth Eastman Dillon &
 Co. Incorporated
 San Francisco, California

Richard D. Bingham
 Drexel Burnham Lambert
 Incorporated
 Los Angeles, California

Thomas W. Borden
 Stone & Youngberg
 San Francisco, California

Charles G. Bragg
 Quincy Cass Associates,
 Incorporated
 Los Angeles, California

Leland S. Bright
 Sage Financial Corporation
 San Francisco, California

Ray E. Hummel
 University Securities
 Corporation
 San Francisco, California

Theodore G. M. Jung
 Bache Halsey Stuart
 Shields Incorporated
 Honolulu, Hawaii

Herbert G. Kawahara
 E. F. Hutton & Company, Inc.
 Los Angeles, California

Ronald P. Lynch
 Lord, Abbett & Co.
 San Francisco, California

Richard A. Miller
 Hornblower, Weeks, Noyes &
 Trask Incorporated
 Los Angeles, California

Jon H. Tolson
 Sutro & Co. Incorporated
 San Francisco, California

Thomas W. Witter
 Dean Witter & Co.
 Incorporated
 San Francisco, California

Theodore F. Schmidt
 Director
 425 California Street,
 Room 1400
 San Francisco, California
 94104

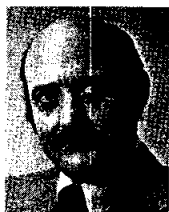
William J. Radding, Jr.
 Director
 606 South Olive Street
 Los Angeles, California
 90014

297 MEMBERS • 976 BRANCH OFFICES • 22,374 REGISTERED REPRESENTATIVES

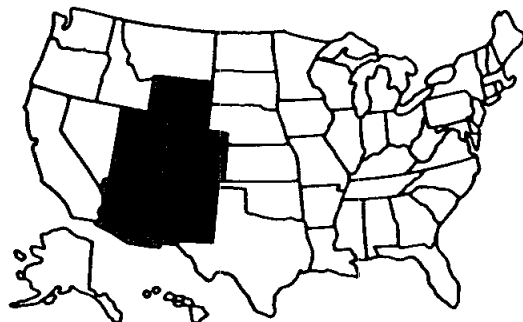
DISTRICT NO. 3

ARIZONA
COLORADO
NEW MEXICO

UTAH
WYOMING



Jordan Mandel
Chairman
Boettcher & Company
Denver, Colorado



David E. Nelson
Vice-Chairman
Prince-Covey & Co., Inc.
Salt Lake City, Utah

William A. Conklin
Bosworth, Sullivan &
Company, Incorporated
Denver, Colorado

John R. Eaker
Quinn & Co., Inc.
Albuquerque, New Mexico

James A. Gamble
Thomson McKinnon Securities
Inc.
Salt Lake City, Utah

Jack I. Kibben
Piper, Jaffray & Hopwood
Incorporated
Sheridan, Wyoming

Edwin J. Pittock
E. J. Pittock & Co. Incorporated
Denver, Colorado

B. Mills Sinclair
Young, Smith & Peacock, Inc.
Phoenix, Arizona

Herve J. R. Tessier
H. J. Tessier & Co., Inc.
Phoenix, Arizona

L. Richard Ure
Dean Witter & Co. Incorporated
Salt Lake City, Utah

John T. Christensen
Director
909 17th Street, Room 608
Denver, Colorado 80202

107 MEMBERS • 324 BRANCH OFFICES • 5,872 REGISTERED REPRESENTATIVES

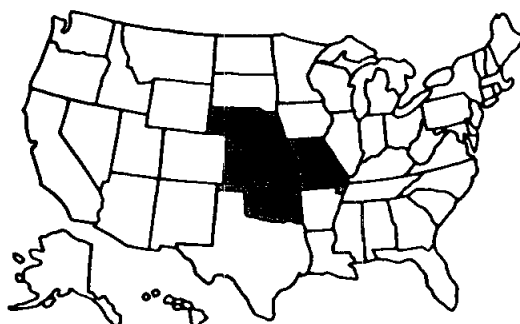
DISTRICT NO. 4

KANSAS
MISSOURI

NEBRASKA
OKLAHOMA



Milton F. Svetanics, Jr.
Chairman
General American Life
Insurance Company
St. Louis, Missouri



Lawrence F. Dendinger
Vice-Chairman
Kirkpatrick, Pettis, Smith,
Polian Inc.
Lincoln, Nebraska

L. Kenneth Britt
Zahner and Company
Kansas City, Missouri

Shelby C. Chism
Burns, Pauli & Co., Inc.
St. Louis, Missouri

Larry S. Gutsch
Dean Witter & Co. Incorporated
Kansas City, Missouri

John H. Henning
Blyth Eastman Dillon & Co.
Incorporated
Kansas City, Missouri

Meredith C. Jones, Jr.
I. M. Simon & Co.
St. Louis, Missouri

Wayne Lamb
Waddell & Reed, Inc.
Kansas City, Missouri

Milton H. Luce, Jr.
Stifel, Nicolaus & Company,
Inc.
Kansas City, Missouri

Douglas V. Martin III
Newhard, Cook & Co., Inc.
St. Louis, Missouri

Walter J. Middlecamp, Jr.
Merrill Lynch, Pierce, Fenner &
Smith Inc.
Kansas City, Missouri

P. David Patrick
Reynolds Securities Inc.
Oklahoma City, Oklahoma

Joseph Pierce
Beecroft, Cole & Company
Topeka, Kansas

Richard M. Coster
Director
911 Main Street, Suite 2230
Commerce Tower Building
Kansas City, Missouri 64105

122 MEMBERS • 370 BRANCH OFFICES • 9,591 REGISTERED REPRESENTATIVES

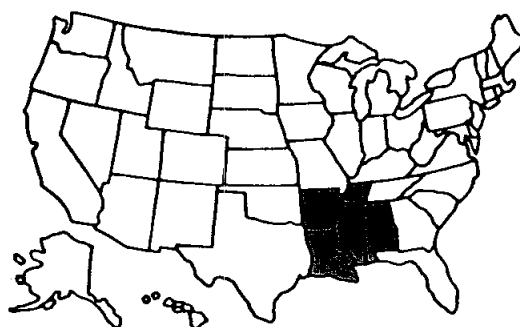
DISTRICT NO. 5

ALABAMA
ARKANSAS
LOUISIANA

MISSISSIPPI
WESTERN TENNESSEE



Lee F. Murphy
Chairman
Paine, Webber, Jackson
& Curtis Incorporated
New Orleans, Louisiana



H. Bradford Walker
Vice-Chairman
Thornton, Farish & Gauntt, Inc.
Montgomery, Alabama

Lee Bodenhamer
Variable Annuity Sales
Corporation
Little Rock, Arkansas

Morris H. Fair
UMIC, Inc.
Memphis, Tennessee

James S. Holbrook, Jr.
First Birmingham Securities
Corporation
Birmingham, Alabama

Frederick Lin Lawrence, Jr.
Tennessee Capital Corporation
Memphis, Tennessee

Hughes Schneidau, Jr.
Waters, Parkerson & Co., Inc.
New Orleans, Louisiana

Leland R. Speed
Leland Speed, Mounger &
Bartlett Incorporated
Jackson, Mississippi

Walter N. Trulock III
Reynolds Securities Inc.
Little Rock, Arkansas

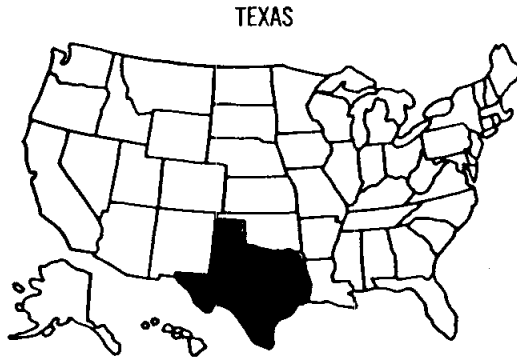
Edward J. Newton
Director
1004 Richards Building
New Orleans, Louisiana 70112

106 MEMBERS • 233 BRANCH OFFICES • 4,528 REGISTERED REPRESENTATIVES

DISTRICT NO. 6



William B. Madden
Chairman
Schneider, Ebernet &
Hickman, Inc.
Dallas, Texas



Jack Ewing Price
Vice-Chairman
Jack Ewing Price & Company,
Inc.
Longview, Texas

William E. Barker, Jr.
Edie Funds
Distributor, Inc.
Dallas, Texas

Raymond W. Burrough
S. E. Freese & Co.
El Paso, Texas

Malcolm L. Cooper
Rotan Mosle Inc.
Austin, Texas

Stanley R. Crowe
Edward D. Jones & Co.
Amarillo, Texas

Daniel D. Howell
E. F. Hutton & Company, Inc.
San Antonio, Texas

Eugene B. Shepherd
Rauscher Pierce Securities
Corporation
Houston, Texas

Peter M. Walker
Director
1610 Metropolitan Federal
Savings Building
1407 Main Street
Dallas, Texas 75202

125 MEMBERS • 354 BRANCH OFFICES • 7,975 REGISTERED REPRESENTATIVES

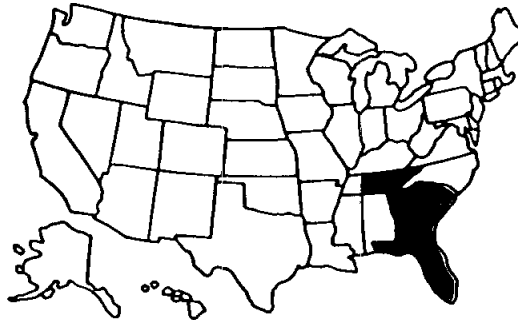
DISTRICT NO. 7

FLORIDA
GEORGIA
SOUTH CAROLINA
EASTERN TENNESSEE

CANAL ZONE
PUERTO RICO
VIRGIN ISLANDS



Ralph W. Williams, Jr.
Chairman
E. F. Hutton &
Company, Inc.
Atlanta, Georgia



Jerry Williams
Vice-Chairman
Jerry Williams, Inc.
Tampa, Florida

William H. Cammack
Equitable Securities
Corporation
Nashville, Tennessee

Andrew B. Carroll
Reynolds Securities Inc.
Fort Lauderdale, Florida

Harold W. Clark
The Cherokee Securities
Company
Nashville, Tennessee

William Hindsman
Johnson, Lane, Space,
Smith & Co., Inc.
Atlanta, Georgia

Walter H. McIntyre, Jr.
A. G. Edwards & Sons, Inc.
Eustis, Florida

Henry R. Sims II
Henry Sims Securities, Inc.
Orangeburg, South Carolina

James L. Spencer
Western Reserve Financial
Services Corp.
Clearwater, Florida

Bennett Whipple
Director
1100 Atlanta Center
250 Piedmont Avenue, N.E.
Atlanta, Georgia 30308

146 MEMBERS • 608 BRANCH OFFICES • 11,523 REGISTERED REPRESENTATIVES

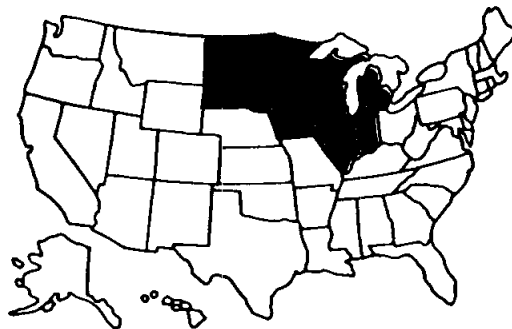
DISTRICT NO. 8

ILLINOIS
INDIANA
IOWA
MICHIGAN

MINNESOTA
NORTH DAKOTA
SOUTH DAKOTA
WISCONSIN



James F. Wade
Chairman
Shearson Hayden
Stone Inc.
Chicago, Illinois



L. Gene Tanner
Vice-Chairman
Raffensperger, Hughes & Co.,
Inc.
Indianapolis, Indiana

J. Philip Boesel, Jr.
R. G. Dickinson & Co.
Des Moines, Iowa

Jerome J. Brault
Burton J. Vincent,
Chesley & Co.
Chicago, Illinois

Clayton F. Brown
Wauterlek & Brown, Inc.
Chicago, Illinois

Arthur J. Cassidy
Wm. C. Roney & Co.
Detroit, Michigan

Mendel J. Engler
Engler & Budd Company
Minneapolis, Minnesota

Paul A. Frederick
Frederick & Company, Inc.
Milwaukee, Wisconsin

Stanley M. Freehling
Freehling & Co.
Chicago, Illinois

Hubert A. Gile, Jr.
The Minnesota Mutual Life
Insurance Company
St. Paul, Minnesota

James M. McMullan
William Blair & Company
Chicago, Illinois

John D. Peterson
City Securities Corporation
Indianapolis, Indiana

Ernest F. Rice, Jr.
Loewi & Co., Incorporated
Milwaukee, Wisconsin

Hal H. Smith III
Smith, Hague & Co.,
Incorporated
Detroit, Michigan

William F. White
Bacon, Whipple & Co.
Chicago, Illinois

E. Craig Dearborn
Director
10 South La Salle Street,
Room 600
Chicago, Illinois 60603

375 MEMBERS • 1,014 BRANCH OFFICES • 33,635 REGISTERED REPRESENTATIVES

DISTRICT NO. 9



Walter R. Chambers, Jr.
Chairman
The Ohio Company
Columbus, Ohio

KENTUCKY OHIO



Lionel P. Greenbaum
Vice-Chairman
Merrill Lynch, Pierce, Fenner &
Smith Inc.
Cleveland, Ohio

Keith R. Barker
Wm. C. Roney & Co.
Cleveland, Ohio

Randolph D. Bucey
The First Boston Corporation
Cleveland, Ohio

H. Garrett Frey
Harrison & Company
Cincinnati, Ohio

Edward S. Herzog
Kidder, Peabody & Co.,
Incorporated
Toledo, Ohio

Jack W. Levi, Jr.
A. E. Aub & Co.
Cincinnati, Ohio

Gilbert L. Pamplin
J. J. B. Hilliard, W. L. Lyons,
Inc.
Louisville, Kentucky

Stephen J. Wolfe
S. J. Wolfe & Co.
Dayton, Ohio

P. William Hotchkiss
Director
100 Erieview Plaza
Cleveland, Ohio 44114

86 MEMBERS • 293 BRANCH OFFICES • 7,287 REGISTERED REPRESENTATIVES

DISTRICT NO. 10

DISTRICT OF COLUMBIA NORTH CAROLINA
MARYLAND VIRGINIA



John W. Rader
Chairman
Wheat, First Securities,
Inc.
Roanoke, Virginia



Beverly B. Munford III
Vice-Chairman
Davenport & Co. of Virginia, Inc.
Richmond, Virginia

Harry M. Boyd
Interstate Securities
Corporation
Charlotte, North Carolina

Edmund J. Cashman, Jr.
Legg Mason Wood Walker,
Inc.
Baltimore, Maryland

George M. Ferris, Jr.
Ferris & Company Incorporated
Washington, D.C.

Marshall H. Johnson
McDaniel Lewis & Co.
Greensboro, North Carolina

John H. Muldowney
Scott & Stringfellow, Inc.
Richmond, Virginia

Jay H. Salkin
Salkin, Welch & Co., Inc.
Lutherville, Maryland

Leslie J. Silverstone
Dean Witter & Co.
Incorporated
Washington, D.C.

Thomas P. Forde
Director
1735 K Street, N.W., 6th Floor
Washington, D.C. 20006

109 MEMBERS • 378 BRANCH OFFICES • 10,963 REGISTERED REPRESENTATIVES

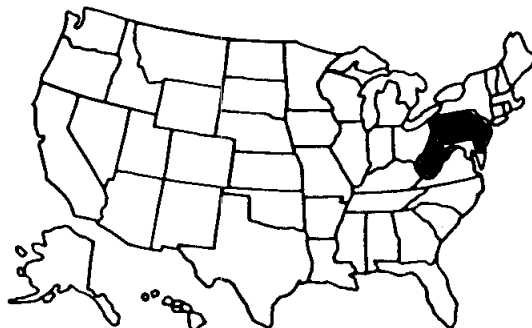
DISTRICT NO. 11

DELAWARE PENNSYLVANIA
NEW JERSEY* WEST VIRGINIA

* With the exception of counties
adjacent to New York City



William M. MacKay
Chairman
Butcher & Singer Inc.
Pittsburgh, Pennsylvania



Henry E. Crouter
Vice-Chairman
DeHaven & Townsend, Crouter
& Bodine, Incorporated
Philadelphia, Pennsylvania

Robert C. Fixter
J. W. Sparks Municipals, Inc.
Philadelphia, Pennsylvania

Frederick H. L. Fung
Harleysville Securities
Corporation
Harleysville, Pennsylvania

Paul A. Hagerty
C. C. Collings and Company Inc.
Philadelphia, Pennsylvania

R. Victor Harned
Warren W. York & Co., Inc.
Allentown, Pennsylvania

L. Edson Mathis, Jr.
Mathis & Co.
Atlantic City, New Jersey

Richard A. Purkiss
Reynolds Securities Inc.
Philadelphia, Pennsylvania

Gerald A. Roney
Moore, Leonard & Lynch,
Incorporated
Pittsburgh, Pennsylvania

Arthur Tresch
A. E. Masten & Co.,
Incorporated
Pittsburgh, Pennsylvania

Allen Weintraub
Advest, Inc.
Philadelphia, Pennsylvania

Robert A. Woerber
Arthurs, Lestrangle & Short
Pittsburgh, Pennsylvania

Robert B. Gilmore
Director
1932 Philadelphia National
Bank Building
Broad and Chestnut Streets
Philadelphia, Pennsylvania
19107

190 MEMBERS • 390 BRANCH OFFICES • 15,548 REGISTERED REPRESENTATIVES

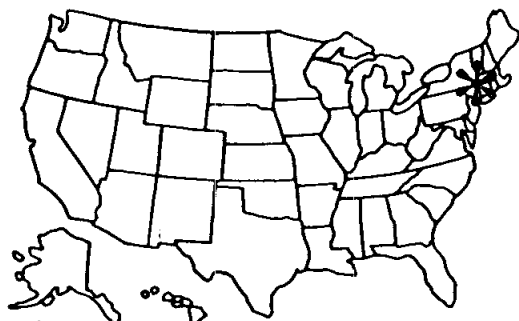
DISTRICT NO. 12

NEW YORK CITY*

* Includes adjacent NY and NJ counties



John C. Printon
Chairman
Printon, Kane & Co.
Summit, New Jersey



Peter A. Bernard
Vice-Chairman
Bache Halsey Stuart Shields
Incorporated
New York, New York

James E. Bacon
White, Weld & Co. Incorporated
New York, New York

Charles A. Bernheim
Stern, Lauer & Co.
New York, New York

Alfred J. Bianchetti
Dean Witter & Co.
Incorporated
New York, New York

Andrew M. Blum
L. F. Rothschild, Unterberg,
Towbin
New York, New York

Donald J. Devine
Freeman Securities Company,
Inc.
Jersey City, New Jersey

John E. Herzog
Herzog, Heine & Co. Inc.
Jersey City, New Jersey

Philip J. Hoblin, Jr.
Shearson Hayden Stone Inc.
New York, New York

Gedale B. Horowitz
Salomon Brothers
New York, New York

Thomas D. Levis
Investors Company
New York, New York

Benjamin L. Lubin
Bruns, Nordeman, Rea & Co.
New York, New York

Daniel J. Lynch
Donaldson, Lufkin & Jenrette
Securities Corporation
New York, New York

David Marcus
Drexel Burnham Lambert
Incorporated
New York, New York

Joseph V. Missett III
Shearson Hayden Stone Inc.
New York, New York

Thomas L. Parker, Jr.
MONY Sales Inc.
New York, New York

Fredric W. Rittereiser
Troster, Singer Corporation
New York, New York

Chester W. Viale
L. F. Rothschild, Unterberg,
Towbin
New York, New York

Stephen S. Wien
M. S. Wien & Co., Inc.
Jersey City, New Jersey

George J. Bergen
Vice President, Director
77 Water Street
New York, New York 10005

805 MEMBERS • 442 BRANCH OFFICES • 32,955 REGISTERED REPRESENTATIVES

DISTRICT NO. 13

CONNECTICUT

MAINE

MASSACHUSETTS

NEW HAMPSHIRE

NEW YORK*

RHODE ISLAND

VERMONT

* With the exception of New York City and adjacent counties



Gilbert M. Lothrop
Chairman
Moors & Cabot
Boston, Massachusetts



James P. Rybeck
Vice-Chairman
Wm. H. Rybeck & Co., Inc.
Meriden, Connecticut

Thomas H. Adams, Jr.
Paine, Webber, Jackson &
Curtis Incorporated
Boston, Massachusetts

Peter N. Dana
White, Weld & Co. Incorporated
Boston, Massachusetts

Donald C. Day
NEL Equity Services
Corporation
Boston, Massachusetts

Frances B. Dyleski
Robert C. Carr & Co., Inc.
Manchester, New Hampshire

Robert L. Goldberg
John Hancock Distributors,
Inc.
Boston, Massachusetts

Chester Hamilton
Fidelity Distributors
Corporation
Boston, Massachusetts

John W. Holt
State Investment-Leonard & Co.
Portland, Maine

N. Michael Keiser
Hugh Johnson & Company, Inc.
Buffalo, New York

George C. McNamee
First Albany Corporation
Albany, New York

W. Lincoln Mossop, Jr.
Barrett & Company
Providence, Rhode Island

Herbert Sarkisian, Jr.
Hodgdon & Company
Boston, Massachusetts

William S. Clendenin
Director
75 Federal Street
Boston, Massachusetts 02110

232 MEMBERS • 488 BRANCH OFFICES • 22,762 REGISTERED REPRESENTATIVES

Purposes

To promote the investment banking and securities business

To standardize its principles and practices

To promote high standards of commercial honor and to promote among members observance of Federal and State securities laws

To provide a medium through which the membership may consult with governmental and other agencies

To cooperate with governmental authority in the solution of problems affecting this business and investors

To adopt and enforce rules of fair practice in the securities business

To promote just and equitable principles of trade for the protection of investors

To promote self-discipline among members

To investigate and adjust grievances between the public and members

