ANNUAL REPORT 1977

National Securities Clearing Corporation

National Securities Clearing Corporation
55 Water Street
New York, New York 10041

ANNUAL MEETING OF SHAREHOLDERS

The Annual Meeting of Shareholders of the Corporation for the election of directors and the transaction of such other business is held on the third Wednesday in April in each year.

INDEPENDENT ACCOUNTANTS

Price Waterhouse & Co.
153 East 53rd Street
New York, New York 10022

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FINANCIAL HIGHLIGHTS

For the Year	1977
REVENUES	$35,527,000
EXPENSES (including taxes)	34,790,000
NET REVENUES	737,000
AVERAGE DAILY VALUE OF TRANSACTIONS SETTLED	$1,551,510,000

At Year End	1977
CLEARING FUND	
ASECC Division	$ 2,655,000
NCC Division	15,816,000
SCC Division	46,450,000

BOARD OF DIRECTORS

Robert M. Flanagan (Chairman)
Executive Vice President
Dean Witter Reynolds Inc.

Joseph Cattivera
Financial Vice President
Morgan, Olmstead, Kennedy & Gardner, Incorporated

Robert T. Eckenrode
Executive Vice President
American Stock Exchange, Inc.

William J. Fields
Executive Vice President & Treasurer
Wheat, First Securities, Inc.

Raymond C. Holland
Senior Vice President
Becker Securities Incorporated

C. Richard Justice
Senior Vice President
National Association of Securities Dealers, Inc.

Donald D. Kittell
Senior Vice President
New York Stock Exchange, Inc.

Robert A. Mackie, Jr.
Executive Vice President
Singer & Mackie, Inc.

Jack Nelson
President
National Securities Clearing Corporation

Gilbert L. Pamplin
Executive Vice President & Treasurer
J. J. B. Hilliard, W. L. Lyons, Inc.

Joseph Racaniello
First Vice President
Drexel Burnham Lambert Incorporated

Robert P. Rittereiser
Regional Vice President
Merrill Lynch, Pierce, Fenner & Smith Inc.

Donald R. Sammet
Senior Vice President
Blunt Ellis & Loewi Incorporated

Paul Underwood
Senior Vice President
E. F. Hutton & Company Inc.

George A. Vonder Linden
First Vice President
Smith Barney, Harris Upham & Co. Incorporated

John D. Weeden
President
Dexter Securities Corporation

BOARD COMMITTEES

Executive Committee

Robert M. Flanagan, Chairman
Jack Nelson
Joseph Racaniello
Robert P. Rittereiser
Donald R. Sammet
Paul Underwood
John D. Weeden

Finance & Audit Committee

Paul Underwood, Chairman
Robert A. Mackie, Jr.
Gilbert L. Pamplin
Robert P. Rittereiser
Donald R. Sammet

Financial Responsibility Committee

Robert P. Rittereiser, Chairman
Raymond C. Holland
Robert A. Mackie, Jr.
Joseph Racaniello
George A. Vonder Linden
John D. Weeden
Paul Underwood - Alternate

Operations Committee

Joseph Racaniello, Chairman
Joseph Cattivera
William J. Fields
Raymond C. Holland
Paul Underwood

1979 NOMINATING COMMITTEE

Charles A. Bernheim
Managing Partner
Stern, Lauer & Co.

Ross L. Cobb
President
Sutro & Co., Incorporated

John F. Curley, Jr.
President
Paine, Webber, Jackson & Curtis Incorporated

Stephen R. Goldenberg
Partner
Goldman, Sachs & Co.

Charles T. Malott
Operations Partner
J. C. Bradford & Co.

Leonard Mayer
Vice President
Mayer & Schweitzer, Inc.

CHAIRMAN'S MESSAGE

As a corporation truly controlled by its users, National Securities Clearing Corporation (NSCC) is pleased to present to its participants the following financial and committee activity reports for 1977. I urge each participant to review the data carefully and refer any questions, comments, or suggestions to the appropriate board and/or staff member.

NSCC was incorporated on March 19, 1976 for the purpose of consolidating the New York City clearance and settlement activities for listed and over-the-counter securities transactions. Nine months later, after extensive proceedings on NSCC's application for registration as a clearing agency, the Securities and Exchange Commission (SEC) granted NSCC's registration on January 13, 1977. NSCC assumed control and responsibility for the operations of the Stock Clearing Corporation, American Stock Exchange Clearing Corporation, and National Clearing Corporation on January 20, 1977.

Progress on the road to the consolidation so ultimately beneficial to the securities industry, however, has not been without some difficulty. In its order granting registration, the SEC specified that certain conditions must be met before the goal of consolidation could be achieved. Satisfaction of these preconditions required that NSCC solicit the cooperation of parties initially opposed to NSCC's creation and the consolidation. Extensive hearings have been conducted by Congress and the SEC to review the progress among the parties as well as the status of the national clearance and settlement system. In addition, suits filed by subsidiaries of Bradford National Corporation against the SEC have raised issues that at this writing are still unresolved by the courts.

I remain convinced that these challenges will be overcome and NSCC will rapidly move towards fulfilling its mandate to respond effectively to the need in the securities industry for lower operating costs and better services for the securities clearance function. Achievement of these goals requires a continuation of the dedication evidenced since its inception by every board and staff member of NSCC. I would like to take this opportunity to thank each one of them, as well as our participants, for their tireless efforts toward improving conditions in our industry.

Robert M. Flanagan

Robert M. Flanagan
Chairman of the Board
May 15, 1978

PRESIDENT'S REPORT

The past year has been one of accomplishment for National Securities Clearing Corporation. In 1977, NSCC completed the necessary tasks associated with the start-up of a new corporation such as assembling and organizing a staff and implementing the necessary policies and procedures to insure an efficient operation. Also during this period, while maintaining its multiple divisional operations, NSCC developed and filed all the necessary rules and procedures with the Securities and Exchange Commission to permit the consolidation of divisional operations and achieved significant progress in satisfying the preconditions to such consolidation as specified by the Commission in its Order granting NSCC's registration.

The major focus of the Corporation during this period has been to overcome the obstacles preventing NSCC from achieving the consolidation of the operations of its three existing divisions. Achievement of operational consolidation will result in savings to the securities industry of some $15 million - $20 million per year and will lead to other significant benefits in terms of broadening participation, enhancing services, and reducing the risks involved in the clearance and settlement of security transactions.

The Commission, in addition to establishing the preconditions to operational consolidation, also restricted NSCC from changing, without their approval, its procedures, rules, or facilities managers until the conditions had been satisfied and required NSCC to offer to establish coordinating groups with other clearing agencies to monitor progress. At this time, eleven of the twelve tasks contained in the preconditions have been accomplished. The lone exception, providing listed processing through the NSCC branch network, could have been accomplished by mid-1977, but the Commission had restricted NSCC from moving forward in this area. These accomplishments were attained in an environment in which NSCC was required to work closely with parties who had opposed NSCC's registration, while maintaining a high level of operational service despite the significant problems created by failure of an NCC Division participant, the power blackout in New York City, and the extreme winter weather.

NSCC's immediate plan, as presented to the Commission in December of 1977 and reasserted in February of this year, is to exercise its contractual right to terminate the NCC Division facilities processor and transfer that processing to the Securities Industry Automation Corporation. This action, it is projected, will result in some $5 million of annual cost savings to NSCC and will provide significant benefits to all participants in terms of in-house savings. At present, NSCC is awaiting action by the Commission on its request.

The consolidation of divisional operations is the last step in merging the three New York City based clearing corporations and an important phase in the development of a national clearance and settlement system. In 1973, the industry itself took the initial step by calling for certain actions that finally resulted in the formation of NSCC. In the past year, through the dedicated efforts of its user Board of Directors and the active support of its participants and their industry organizations, NSCC has reached the threshold of achieving its immediate goal. We are confident that the momentum gained will be maintained and the forecasted efficiencies of the merger and ultimately the national system will soon begin to be realized.

Jack Nelson
President
May 15, 1978

OPERATIONS COMMITTEE REPORT

A major function of the Operations Committee is the on-going review of all NSCC operations. In this regard considerable Committee and staff effort has been devoted to monitoring the quality of service being provided to participants by the Corporation's two facilities managers. Based upon participant comments to NSCC and upon the Committee's on-going review of operations, these monitoring efforts have been directed primarily to the level of service being provided to NCC Division participants.

The Committee is also involved in the planning process where it reviews proposals for new and improved services and provides "user input" to the development cycle. Although the major effort in this area during the past year was directed towards satisfying the pre-consolidation conditions imposed upon NSCC as part of the SEC's Order granting registration, there were also several new and improved services instituted. Among these are:

A. Expanded Special Representative Category.

NSCC expanded its Special Representative category in the SCC Division to include any clearing member or registered clearing agency. This permits a Special Representative to submit transaction data to NSCC when the Special Representative is acting for either a participant or a non-participant, and therefore, it allows the Special Representative to clear transactions more efficiently where it is acting as an executing agent for another broker/dealer.

B. Expanded Interfaces.

The clearing interfaces were expanded to include the addition of options exercises and assignments through the SCC Division Continuous Net Settlement system, and to include listed bonds.

C. Provided Issuers with Listing of NCC & Co. Holders.

This service provides to issuers, upon their request, a listing of NCC Division participants who are the holders of an issuer's stock registered in the name of NCC & Co. (NSCC's nominee name) and maintained by NSCC in bulk. This service provides the issuers with names and mailing addresses of the NSCC-NCC Division participants and the number of shares being held for each participant in NCC & Co. name at NSCC.

D. Consolidated Contract Lists.

SCC Division contract lists were consolidated in two areas. The first was the inclusion of New York Stock Exchange (NYSE) odd lot transactions on the list of SCC Division contracts for round lot transactions; the second allowed for the SCC Division bond contract lists to also include American Stock Exchange (ASE) bond transactions. In both cases, the membership realized the benefit of consolidated processing of listed (NYSE, ASE) transactions. Also, the addition of ASE bond transactions to SCC contracts allowed for the processing of listed bond transactions through the clearing interfaces.

E. Facilitated Rebate of New York State Stock Transfer Tax.

NSCC, in conjunction with New York State, implemented the first steps leading to the phasing out of the stock transfer tax. This first phase, which allowed for a 50% rebate to non-New York residents, began on October 1, 1977. For the quarter ending December 31, 1977, in excess of $9.5 million was funneled between the participants, the Clearing Corporation, and the State, in order to comply with the new rebate procedures.

Since mid-1977, the Corporation has been restricted by the SEC from undertaking the development of new services, and thus has been prohibited from developing several significant services that have been requested by the industry. Once these restrictions are removed, NSCC plans to move forward with the development of these projects.

Significant daily average volume statistics for the year 1977 are listed on the following page.

Joseph Racaniello, Chairman
Operations Committee
May 15, 1978

VOLUME — DAILY AVERAGES

Value of Transactions Settled	$1,551,510,000
Dollar Settlement	$ 354,674,000
Stock Transactions — Compared Items	63,335
Stock Transactions — Compared Shares	27,637,000
Stock Transactions — Compared Value	$ 658,525,000
Bond Transactions — Compared Items	3,415
Bond Transactions — Compared Bonds	159,410
Bond Transactions — Compared Value	$ 143,704,000
Envelope Settlement Service — Items	13,345
Envelope Settlement Service — Value	$1,106,598,000
National Envelope Settlement Service — Items	100
National Envelope Settlement Service — Value	$ 697,000
Correspondent Delivery and Collection Service — Items	240
Correspondent Delivery and Collection Service — Value	$ 25,320,000
Dividend Settlement Service — Items	480
Dividend Settlement Service — Value	$ 317,000
National Transfer Service — Items	4,895
Clearing Interfaces — Incoming Items	4,135
Clearing Interfaces — Incoming Shares	3,125,000
Clearing Interfaces — Outgoing Items	2,065
Clearing Interfaces — Outgoing Shares	657,000

FINANCIAL RESPONSIBILITY COMMITTEE REPORT

The function of the Financial Responsibility Committee is to review the administration of the Corporation's rules and stated policies with respect to qualifications for initial and continued participation as well as dismissal and disciplinary actions. In addition, it reviews and makes recommendations to the Board of Directors regarding proposed changes in or interpretations of rules relating to participants. Finally, the Committee serves as an appeal board for participants or applicants for membership wishing to register a grievance against the Corporation for its actions or the operation of its various services.

As part of the Committee's ongoing responsibility regarding the financial accountability of participants, it was involved quite actively during 1977 in settling matters relating to Swift, Henke & Co., Inc. Liquidation of the open positions at NSCC of this participant resulted in a loss of $867,000. No assessment was made against the participants' Clearing Fund, however, as the NSCC board determined to satisfy the loss from operating revenues. The Corporation has filed a claim for these monies against the Estate of Swift, Henke & Co., Inc., which is the subject of SIPC proceedings.

Finally, the Committee is engaged in major development projects expected to be completed in 1978 concerning the consolidation of the three divisions' surveillance functions, financial accountability rules, and Clearing Funds.

Robert P. Rittereiser, Chairman
Financial Responsibility Committee
May 15, 1978

FINANCE AND AUDIT COMMITTEE REPORT

The function of the Finance and Audit Committee is to monitor the financial integrity and viability of the Clearing Corporation. This is accomplished through periodic review of financial budgeting and performance data, by conducting an active external and internal financial audit program, and by lending counsel and support to the internal NSCC Finance and Audit functions.

As of December 31, 1977, retained earnings were $737,000, a major step toward attaining the goal of $2,000,000 in working capital reserve established during the year by NSCC's user board. It was determined that this level of working capital would be appropriate to protect the membership against short term operating losses caused by a period of sustained low volume, and to provide for the development of new systems.

Under NSCC's proposed pricing plan, earnings would be retained for working capital purposes on a graduated basis until such time as a level of $2,000,000 in retained earnings is attained. After reaching this level, all revenue in excess of expenses would be rebated proportionately to the participants.

Two items offset the Corporation's favorable financial performance during the year. A significant loss resulted from the financial impairment of a participant in the NCC Division, which is discussed in more detail in the Financial Statements and in the report of the Financial Responsibility Committee. The other major unbudgeted expense item in 1977 was legal fees in excess of $200,000 incurred substantially in defense of the challenge to the SEC's registration of NSCC as a clearing agency. These expenditures were necessitated by two suits brought against the SEC by wholly owned subsidiaries of Bradford National Corporation, the facilities processor for the NCC Division. These factors combined increased expenses by $1,104,000.

It should also be pointed out that elimination of Interface Fees this past summer resulted in decreased billings to participants of approximately $280,000. These fees were eliminated at the request of the SEC and will be the subject of future SEC hearings.

Another financial responsibility of the Clearing Corporation is the safekeeping of the Clearing Fund deposits. These deposits totalled $64,921,000 at year end and consisted of $7,914,000 in cash and $57,007,000 collateralized by federal and state obligations with a market value of $69,734,000. This collateral is deposited according to the rules of NSCC's three divisions and kept under the control of the Corporation to act as a buffer against potential participant impairment. The cash in this fund, with the exception of the portion attributable to the NCC Division participants' contributions, along with other temporarily available cash, is invested in federal obligations in order that interest earnings may be realized. This procedure effectively results in lower fees to participants. The benefits from the use of the NCC Division Clearing Fund cash accrue to Bradford National Corporation under the facilities management contract, and are not available to NSCC. Interest earnings at NSCC were $406,000 in 1977.

Operating costs of processing over one and one-half billion dollars of daily settlement activity are carefully controlled. Although the Corporation has no basis for comparison with income statements of prior years, data from the predecessor clearing corporations are available which demonstrate that costs are reasonable, though of course subject to areas of escalation common to most businesses. In this regard, SIAC, the Corporation's facilities processor for listed securities, had a relatively insignificant increase over 1976 of approximately $130,000 in costs or 1% on a base of over $13,000,000. Under the Bradford contract, NCC Division costs are based on a percentage of revenue and thus vary with volume fluctuations.

Paul Underwood, Chairman
Finance and Audit Committee
May 15, 1978

NATIONAL SECURITIES CLEARING CORPORATION

BALANCE SHEET

	December 31, 1977	January 1, 1977
ASSETS		
Current assets:		
Cash	**$ 5,666,000**	$ 603,000
Temporary investments	**7,913,000**	6,081,000
Accounts receivable, less allowance for doubtful accounts of $867,000 at December 31, 1977 (Note 6)	**3,301,000**	2,041,000
Settlement accounts receivable	**5,173,000**	22,855,000
Other current assets	**27,000**	116,000
Total current assets	**22,080,000**	31,696,000
Clearing fund (Note 3)	**57,007,000**	60,288,000
Furniture, equipment & leasehold improvements, net of accumulated depreciation and amortization of $181,000 at December 31, 1977	**340,000**	410,000
Other noncurrent assets	**25,000**	39,000
	$79,452,000	$92,433,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	**$ 3,097,000**	$ 1,692,000
Regulatory fee payable (Note 4)	**954,000**	626,000
Settlement accounts payable	**7,774,000**	20,212,000
Accrued taxes and other expenses	**461,000**	4,000
Unclaimed dividends	**608,000**	377,000
Total current liabilities	**12,894,000**	22,911,000
Clearing fund (Note 3)	**64,921,000**	68,622,000
Commitments and contingent liabilities (Notes 7, 8, 10 and 12)		
	77,815,000	91,533,000
Shareholders' equity:		
Common stock, authorized, issued and outstanding, 30,000 shares of $.50 par value	**15,000**	15,000
Capital in excess of par	**885,000**	885,000
Retained earnings (Note 1b)	**737,000**	—
	$79,452,000	$92,433,000

The accompanying notes to financial statements are an integral part of this statement.

NATIONAL SECURITIES CLEARING CORPORATION

INCOME STATEMENT
FOR THE YEAR ENDED DECEMBER 31, 1977

(Note 1a)

Revenue from clearing services	$35,121,000
Interest income	406,000
	35,527,000
Expenses:	
Securities Industry Automation Corporation processing fees (Notes 4 and 5)	13,529,000
Bradford National Corporation processing fees (Note 5)	8,946,000
The Depository Trust Company fees	4,571,000
Regulatory fees (Note 4)	3,583,000
General and administrative	1,094,000
Employee compensation and related benefits	1,034,000
	32,757,000
Income before other expenses and income taxes	2,770,000
Other expenses:	
Unallocated settlement loss (Note 6)	867,000
Litigation expense (Note 12)	237,000
Income before income taxes	1,666,000
Provision for taxes on income	929,000
Net income (Note 1b)	$ 737,000

The accompanying notes to financial statements are an integral part of this statement.

STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEAR ENDED DECEMBER 31, 1977

(Note 1a)

Financial resources were provided by:	
Net income	$ 737,000
Add — Income charges not affecting working capital in the period:	
Depreciation and amortization	56,000
Write-off of furniture and equipment	26,000
	819,000
Working capital provided from operations:	
Reimbursement for depreciation and amortization from Bradford National Corporation	135,000
Other	4,000
	958,000
Financial resources were used for:	
Decrease in clearing fund	(420,000)
Acquisition of furniture, equipment and leasehold improvements	(137,000)
Increase in working capital	$ 401,000

ANALYSIS OF CHANGES IN WORKING CAPITAL

Increase (decrease) in current assets:	
Cash	$ 5,063,000
Investments	1,832,000
Accounts receivable	1,260,000
Settlement accounts receivable	(17,682,000)
Other current assets	(89,000)
	(9,616,000)
(Increase) decrease in current liabilities:	
Accounts payable	(1,405,000)
Regulatory fee payable	(328,000)
Settlement accounts payable	12,438,000
Accrued taxes and other expenses	(457,000)
Unclaimed dividends	(231,000)
	10,017,000
Increase in working capital	$ 401,000

The accompanying notes to financial statements are an integral part of this statement.

NATIONAL SECURITIES CLEARING CORPORATION

NOTES TO FINANCIAL STATEMENTS

NOTE 1 — Summary of Significant Accounting Policies:

(a) *Incorporation:*

On January 13, 1977, the application of National Securities Clearing Corporation (the Company) for registration as a clearing agency was approved by the Securities and Exchange Commission (SEC). This application called for the consolidation of Stock Clearing Corporation (SCC), (a wholly owned subsidiary of the New York Stock Exchange), American Stock Exchange Clearing Corporation (ASECC), (a wholly owned subsidiary of the American Stock Exchange) and National Clearing Corporation (NCC), (a wholly owned subsidiary of the National Association of Securities Dealers) into the Company, which, on January 20, 1977, assumed the operations of the three clearing facilities retroactive to the opening of business on January 1, 1977, as further described in Note 2. The Company was incorporated in March 1976 and incurred prior to January 1, 1977 approximately $113,000 of start-up costs which have been expensed in the accompanying income statement. These costs were included in other assets on the January 1, 1977 opening balance sheet pending approval for the Company to operate as a registered clearing agency.

(b) *Retained earnings:*

The Company is attempting to establish a contingency fund from its revenue, but in general does not propose to earn profits or declare dividends. The net income for 1977 was retained for this purpose.

(c) *Cash:*

Substantially all of the Company's cash represents items in process for collection or restricted for settlement transactions.

(d) *Clearing Fund:*

The Company records the Clearing Fund based on cash deposited in the fund and amounts callable on demand, which are secured by securities issued or guaranteed by the United States, its states and political subdivisions. Interest income on such securities accrues to the clearing members.

(e) *Temporary investments:*

Temporary investments are valued at cost which approximates market and consist of U.S. Treasury Bills and U.S. Treasury Bills purchased under agreements to resell. The Board of Directors has mandated that investments cannot exceed a maturity of five years from date of purchase.

(f) *Settlement accounts:*

Settlement accounts receivable and payable arise from temporary time lags in the cash settlement process between the Company and clearing members, non-member participants, other clearing organizations, depositories or dividend disbursing agents.

(g) *Furniture, equipment and leaseholds:*

Furniture, equipment and leaseholds are stated at cost. These are substantially leasehold improvements at 55 Water Street and fixed assets transferred from NCC, primarily located at 2 Broadway.

When properties are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts with any resulting gain or loss reflected in income. Major betterments are capitalized while maintenance and repairs are expensed in the year incurred.

(h) *Depreciation and amortization:*

The Company provides for depreciation of furniture and equipment and amortization of leasehold improvements on a straight-line basis over the estimated life of the asset and over the term of the lease or the life of the asset, whichever is shorter, respectively.

(i) *Income taxes:*

Income taxes are based on pre-tax financial statement income with an appropriate deferred tax provision of $27,000 to provide for the tax effect of temporary timing differences between pre-tax financial statement income and taxable income; i.e., Treasury Bill income is accrued for financial statement purposes, but not for tax purposes, and depreciation is calculated using accelerated methods for tax purposes.

NOTE 2 — History and Organization:

As a result of the consolidation of the three clearing facilities into the Company, NCC agreed to transfer $900,000 of its net assets to the Company in exchange for a one-third ownership in the Company and a note receivable for $600,000 bearing interest at 6.25% which was paid when due on September 15, 1977. The net assets transferred to the Company represented all net assets of NCC except certain cash balances and a liability for pension contributions. In addition, the Company assumed the responsibility for NCC's leases and contracts, including a contract involving certain operations with Bradford (See Note 5). SCC and ASECC each contributed $300,000 in cash as their one-third capital interest. As part of this transaction, ASECC's and SCC's assets and liabilities related to the Clearing Fund, settlement accounts and the receivables and payables which arise as a result of the Continuous Net Settlement (CNS) system were transferred to the Company. The Company is managed by its own staff and guided by an independent user Board of Directors which is responsible for its policies, operations and financing.

The Company offers to all participants all the services formerly offered by SCC, ASECC and NCC. The Company's fees to participants are set by the Board of Directors and are based on the cost of providing its services.

NOTE 3 — Clearing Fund:

The operating rules of the Company require each clearing member to maintain an amount on deposit in the Clearing

NOTES (continued)

Fund before such member can participate in the Company's settlement system.

The composition of the fund is as follows:

	1977 December 31	1977 January 1
Cash	$ 7,914,000	$8,334,000
Amounts due from members on demand — generally secured by U.S. Government and Municipal obligations (market value $69,734,000 and $67,424,000, respectively)	57,007,000	60,288,000
	$64,921,000	$68,622,000

The Company is permitted to use the cash deposited by the SCC and ASECC members to fulfill settlement obligations when necessary. Also, the Company may invest the cash deposited by the SCC and ASECC Divisions in short-term investments. Such cash deposits amounted to $4,393,000 and $4,249,000 at December 31, 1977 and January 1, 1977, respectively.

NOTE 4 — Transactions with Related Parties:

Amounts billed for regulatory services to the Company during 1977 by the New York Stock Exchange (NYSE), the American Stock Exchange (Amex) and the National Association of Securities Dealers (NASD) and amounts unpaid at December 31, 1977 are as follows:

	NYSE	Amex	NASD	Total
Billed	$2,525,000	$484,000	$574,000	$3,583,000
Unpaid at December 31, 1977	662,000	122,000	170,000	954,000

The regulatory services provided include periodic examinations of the records and operations of clearing members, the monitoring and investigation of the financial and operating condition of clearing members and new applicants for membership, as well as notification to the Company of unusual market conditions which may affect securities cleared.

As described in Note 5, the Company entered into a facilities management agreement with SIAC which is owned by the NYSE and Amex. The Company also entered into a rental agreement for office space with SIAC through 1978 with an option to renew for an additional three years. Payments to SIAC under this agreement amounted to $91,000 during 1977. The NYSE also owns a minority interest in The Depository Trust Company, whose facilities are used by the Company.

NOTE 5 — Facilities Management Agreements:

Under the terms of an agreement with Bradford, which extends through September, 1979, Bradford has agreed to provide the necessary facilities, personnel and services in support of certain of the Company's clearing services and related functions for the NCC Division. Bradford's fee under this agreement ranges from 80% to 84% of the applicable monthly revenue with the balance retained by the Company; however, the Company's minimum monthly share is not to be less than $70,000. This agreement may be cancelled by NSCC without penalty upon 90 day written notice to Bradford. The Securities and Exchange Commission Order granting NSCC's registration requires SEC approval prior to notice of termination to Bradford until such time as all preconditions contained in such Order are satisfied. In addition, Bradford reimbursed the Company in 1977 for depreciation and amortization of certain assets totalling $135,000.

Also, on January 1, 1977, the Company entered into a facilities management agreement with SIAC whereby SIAC provides the necessary facilities, personnel and services in support of certain of the Company's clearing services and related functions for the SCC and ASECC Divisions. SIAC's fee consists of all costs arising from providing such services including all direct costs, computer costs and general overhead. The agreement is for the five-year period ending December 31, 1981, and is renewable in the absence of notice of cancellation by either party. The agreement may be cancelled after two years upon a monthly payment of $225,000 for the remaining term of the initial five-year period.

NOTE 6 — Unallocated Settlement Loss:

The Company's agreement with the NCC Division's Clearing Fund members provides that settlement losses be allocated to the membership. As a result of one member's inability to settle his security trades, the Company incurred a net loss of $867,000. In June, 1977, the Board of Directors of the Company decided to absorb the loss rather than allocate it to its clearing members through the Clearing Fund. The Company has filed a claim against the estate of the member but recovery, if any, cannot be presently assessed.

NOTE 7 — Rental Commitments:

Rent expense in 1977 was $108,000. The minimum non-cancellable rental commitments for office space are as follows:

Year	Rental Commitment	Bradford Reimbursement under a Sublease	Sublease
1978	$771,000	$650,000	$6,000
1979	216,000	215,000	
1980	1,000		

NOTES (continued)

NOTE 8 — Contingencies (See also Note 12):

The Continuous Net Settlement (CNS) system interposes the Company with a member in each daily security settlement. The total long and short security settlements are in balance each day.

The failure of a member to deliver a security to the Company, and the corresponding failure by the Company to redeliver such securities to its members, will result in unsettled transactions. Unsettled CNS transactions are marked to market and charged or credited daily to the members involved.

At December 31, 1977, there was a total of approximately $316 million ($340 million at January 1, 1977) of unsettled transactions.

NOTE 9 — Income Taxes:

Total income tax expense amounted to $929,000 (an effective rate of 55.8%). The following is a reconciliation of this effective rate with the federal statutory income tax rate of 48%:

Statutory Rate	48.0%
State and local income taxes (net of federal income tax benefit)	9.2
Other	(1.4)
	55.8%

NOTE 10 — Pension Plan:

In 1977, the Company made its initial payment to a trusteed non-contributory pension plan which covers substantially all of its employees. The Company's policy is to fund pension cost accrued. The total pension expense for the year was $39,000 which includes amortization of past service costs.

As at December 31, 1977, the liability for unfunded past service costs amounted to $121,000. This liability is being funded over a period of 10 years. The actuarially computed vested benefits exceeded the pension fund net assets at December 31, 1977 by $55,000.

NOTE 11 — Interest Income:

Interest income in 1977 totalled $406,000. Such income was earned from investments in repurchase agreements and U.S. Treasury Bills which earned an average rate of 5.56% and 5.27% during the year, respectively.

NOTE 12 — Litigation:

As described in Note 1a, the Company became a registered clearing agency upon approval by the Securities and Exchange Commission. Two suits have been brought challenging final orders of the Securities and Exchange Commission. The first suit challenges the Commission's final order which granted the Company's registration as a clearing agency. The second suit challenges the Commission's final order approving two operational rule changes of the Company. The Commission is contesting each of these suits and the Company has intervened in each suit in support of the Commission. While the outcome of these suits is unknown at this time, management is not anticipating an adverse effect on the financial condition of the Company.

Report of Independent Accountants

Price Waterhouse & Co.

153 EAST 53RD STREET
NEW YORK, N.Y. 10022
212-371-2000

April 18, 1978

To the Board of Directors of
National Securities Clearing Corporation

In our opinion, the accompanying balance sheets and the related statements of income and of changes in financial position present fairly the financial position of National Securities Clearing Corporation at December 31, 1977 and January 1, 1977, and the results of its operations and the changes in its financial position for the year ended December 31, 1977, in conformity with generally accepted accounting principles. Our examinations of these statements 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.

Price Waterhouse & Co.

PARTICIPANTS OF NATIONAL SECURITIES CLEARING CORPORATION

ABD Securities Corp.
Adams, Harkness & Hill, Inc.
Adler, Coleman & Co.
Advest, Inc.
Allen & Co., Inc.
Amalgamated Bank of New York
American Securities Corp.
Amivest Corporation
Amswiss International Corp.
Anderson & Strudwick, Inc.
Arnhold & S. Bleichroeder, Inc.
Asiel & Co.
Atlantic Capital Corporation
Babbitt, Meyers & Company, Inc.
Bache Halsey Stuart Shields Incorporated
Bacon, Whipple & Co.
Baird, Patrick & Co., Inc.
Bank Leumi Trust Company of New York
Bank of Montreal (Agency)
Bank of Montreal Trust Co.
Bank of New York (The)
Bankers Trust Company
Baum, George K., & Company Incorporated
Bear, Stearns & Co.
Beauchamp & Co.
Becker Securities Incorporated
Beecroft, Cole & Co.
Bell & Beckwith
Bellamah, Neuhauser & Barrett, Inc.
Benton, Tompane & Co.
Bernstein (Sanford C.) & Co., Inc.
Blair (William) & Company
Blunt Ellis & Loewi Incorporated
Blyth Eastman Dillon & Co. Incorporated
Boenning & Scattergood Inc.
Boesky (Ivan F.) and Company
Boettcher and Company
BOSECO, Inc.
Boston Stock Exchange Clearing Corporation
Bradford (J. C.) & Co.
Bradford Securities Processing Services, Inc.
Bradford Trust Company
Branch, Cabell & Co.
Brown (Alex.) & Sons
Brown Brothers Harriman & Co.
Brown & Company Securities Corporation
Bruns, Nordeman, Rea & Co.
Burgess & Leith Incorporated
Burns Fry and Timmins Inc.
Burns, Pauli & Co., Inc.
Butcher & Singer Inc.
Canadian Depository for Securities Limited (The)
Canadian Imperial Bank of Commerce
Cantor, Fitzgerald & Co., Inc.
Cantor (S. B.) Co., Inc.
Carmcley Corporation
Carolina Securities Corporation
Carr Securities Corporation
Carr & Thompson, Inc.
Cartwright (L.) & Co.
CBT Clearing Corp.
Chapin, Davis and Co., Inc.
Chase Manhattan Bank, N.A.
Chemical Bank
Chicago Corporation (The)
Christopher (B. C.) & Company
Citibank, N.A.
Colin, Hochstin Co.
Conklin, Cahill & Co.
Conning & Co.
Cook Investment Co.
Cowen & Co.
Craig-Hallum, Inc.
Dain, Kalman & Quail, Incorporated
Daiwa Securities America Inc.
Davenport & Co. of Virginia, Inc.
Davis (Shelby Cullom) & Co.
deCordova, Cooper & Co.
DEFCO Securities Inc.
Deltec Securities Corporation
Dexter Securities Corporation
Dickinson (R. G.) & Co.
Dillon, Read & Co., Inc.
Doft & Co., Inc.
Dominick Investor Services Corporation
Donaldson, Lufkin & Jenrette Securities Corporation
Drexel Burnham Lambert Incorporated
Dritz Goldring Wohlreich & Co.
Drysdale Securities Corporation
Eastern Securities Inc.
Easton & Co.
Eberstadt (F.) & Co., Inc.
Edwards (A. G.) & Sons, Inc.
Einhorn & Co.
Elkins, Stroud, Suplee & Co.
Engler & Budd Company
Eppler, Guerin & Turner, Inc.
Equitable Securities Corporation
Equity Securities Trading Co. Inc.
Ernst & Company
EuroPartners Securities Corporation
Evans & Co., Incorporated
Execution Services Incorporated
Fagenson & Company, Inc.
Fahnestock & Co.
Ferris & Company, Incorporated
Fidelity Union Trust Co.
Fiduciary Trust Company of New York

PARTICIPANTS OF NATIONAL SECURITIES CLEARING CORPORATION

Financial America Securities, Inc.
First Albany Corporation
First Boston Corporation (The)
First Independent Stock Transfer Agent, Inc.
First Jersey National Bank
First Jersey Securities, Inc.
First Manhattan Co.
First of Michigan Corporation
First National Boston Clearance Corp.
First Southwest Company
First Wall Street Settlement Corporation
Flagship First National Bank
Folger Nolan Fleming Douglas Incorporated
Foster & Marshall Inc.
Fowler & Rosenau
Frank (Walter N.) & Co.
Frankel (Wm. V.) & Co., Incorporated
Freehling & Co.
Freeman Securities Company, Inc.
French American Banking Corp.
Fried (Albert) & Company
Gintel & Co.
Goldman, Sachs & Co.
Goldstein (M.E.) & Co., Inc.
Gowell Securities Corporation
Gradison & Company Incorporated
Granger & Company
Gruntal & Co.
Gruss (Oscar) & Son Incorporated
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Hartford National Bank and Trust Company
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Henderson, Harrison & Co.
Herzfeld & Stern
Herzog, Heine, Geduld, Inc.
Hill, Thompson, Magid & Co., Inc.
Hilliard (J. J. B.), Lyons (W. L.), Inc.
Hirshon, Roth & Co.
Hopper Soliday & Co., Inc.
Howard, Weil, Labouisse, Friedrichs Incorporated
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Hummer (Wayne) & Co.
Hutton (E. F.) & Company Inc.
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Ingalls & Snyder
Institutional Equity Corporation
Interstate Securities Corporation
Irving Trust Company
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Janney Montgomery Scott Inc.
Johnson, Lane, Space, Smith & Co., Inc.
Johnston, Lemon & Co., Incorporated
Jones (Edward D.) & Co.
Josephthal & Co. Incorporated
Kalb, Voorhis & Co.
Kaufmann, Alsberg & Co.
Kidder, Peabody & Co. Incorporated
Kingsley, Boye & Southwood, Inc.
Krieger (Henry) & Co.
La Branche & Co.
Laidlaw Adams & Peck Inc.
Lang and Company
Lasker, Stone & Stern
Lawrence (Cyrus J.) Incorporated
Lawrence, O'Donnell & Co.
Lazard Freres & Co.
Lenart, McHugh & Co.
Lewco Securities Corp.
Lincoln First Bank of Rochester
Mabon, Nugent & Co.
Madoff, Bernard L.
Magid (D. H.) & Co., Incorporated
Manley, Bennett, McDonald & Co.
Manufacturers Hanover Trust Company
Manufacturers & Traders Trust Company
Marcus Schloss & Co., Inc.
Marine Midland Bank - New York
Marks (Carl) & Co., Inc.
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McDonald & Company
Meehan (M. J.) & Co.
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Mesirow & Company
Midsouthwest Securities, Inc.
Midwest Clearing Corporation
Mitchel, Schreiber, Watts & Co., Inc.
Moore, Leonard & Lynch, Incorporated
Moore & Schley, Cameron & Co.
Morgan Guaranty Trust Company of New York
Morgan, Keegan & Company, Inc.
Morgan, Olmstead, Kennedy & Gardner Incorporated
Morgan Stanley & Co. Incorporated
Morrissey (F. J.) & Co.
Muir (John) & Co.
Muller & Company
Murphey, Marseilles & Smith
Murphy & Durieu
National Bank of North America
Neuberger & Berman
Neuberger Securities Corporation
Newbold's (W. H.) Son & Co. Inc.

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Parker, Weissenborn & Moynahan, Inc.
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Pforzheimer (Carl H.) & Co.
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Prescott, Ball & Turben
Purcell, Graham & Co., Inc.
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Quinn (E. J.) & Co., Inc.
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Regis Management Corporation
Reich & Co., Inc.
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Richardson Securities, Inc.
Riviere Securities Corporation
Robb, Peck, McCooey & Co., Inc.
Robertson, Colman, Siebel & Weisel
Robinson-Humphrey Company, Inc. (The)
Rodman & Renshaw, Inc.
Roney (Wm. C.) & Co.
Rose & Company Investment Brokers, Inc.
Rotan Mosle Inc.
Rothschild (L. F.), Unterberg, Towbin
Roulston & Company, Inc.
Rowland (R.) & Co. Incorporated
Ryan (John J.) & Co.
Sade & Co.
Salkin, Welch and Co., Inc.
Salomon Brothers
Schapiro (M. A.) & Co., Inc.
Scherck, Stein & Franc, Inc.
Schroder Trust Co.
Securities Settlement Corporation
Seligman (J. & W.) & Co.
Shaine (H. B.) & Co., Inc.
Shawmut Securities Clearance Corp.
Shearson Hayden Stone Inc.
Simon (I. M.) & Co.
Singer & Mackie, Inc.
Smith Barney, Harris Upham & Co. Incorporated
Smith (E. H.) Jacobs & Co.
Smith (E. W.) Co.
Spear, Leeds & Kellogg
State Street Bank & Trust Company
Steichen (R. J.) & Co.
Stephens, Inc.
Stern Brothers & Co.
Stern & Kennedy
Stern, Lauer & Co.
Sterne, Agee & Leach, Inc.
Stifel, Nicolaus & Company Incorporated
Stillman, Maynard & Co.
Stix & Co., Inc.
Stock Clearing Corporation
Stock Clearing Corporation of Philadelphia
Stokes, Hoyt & Co.
Streicher (J.) & Co.
Stuart Brothers
Suez American Corporation
Sutro & Co. Incorporated
Swiss American Securities Inc.
Swiss Bank Corporation
Tennessee Securities, Inc.
Thomson McKinnon Securities Inc.
Toronto-Dominion Bank, The
Tucker, Anthony & R. L. Day, Inc.
Tweedy Browne Clearing Corporation
United Americas Bank
United Missouri Bank of Kansas City, N.A.
United States Trust Company of New York
Vincent (Burton J.), Chesley & Co.
Viner (Edward A.) & Co., Inc.
Wagner, Stott & Co.
Wallach (D. H.), Inc.
Weber, Hall, Cobb & Caudle, Inc.
Wechsler & Krumholz, Inc.
Wedbush, Noble, Cooke, Inc.
Weeden & Co. Incorporated
Weiss, Peck & Greer
Wellington & Co.
Wells Fargo Securities Clearance Corporation
Westminster Securities Corp.
Wheat, First Securities, Inc.
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Wien (M. S.) & Co., Inc.
Williams (C. T.) & Co., Inc.
Williams (Jerry), Inc.
Witter (Dean) Reynolds Inc.
Wood Gundy Incorporated
Wreszin, Prosser, Romano & Co.
Yamaichi International (America), Inc.
Young, Smith & Peacock, Inc.

The above listed firms are participants of National Securities Clearing Corporation as defined by the Securities and Exchange Act of 1934. Other organizations use certain limited services offered by NSCC. For a complete listing of services provided and member participants, please write to the Director of Membership, NSCC, 55 Water Street, New York, New York 10041.
Data compiled as of May 15, 1978.

OFFICERS OF NATIONAL SECURITIES CLEARING CORPORATION

Robert M. Flanagan
Chairman of the Board

Jack Nelson
President

John F. Elberfeld
Vice President, Finance and Administration
Treasurer

John J. Quirke
Vice President, Marketing

Robert A. Schultz
Vice President, Planning and Operations

Robert J. Woldow
Vice President and General Counsel
Secretary

David F. Hoyt
Assistant Secretary

Alvin W. McGee
Assistant Treasurer

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Cleveland, Ohio 44115

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Jersey City, New Jersey 07302

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New York, New York 10004

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Philadelphia, Pennsylvania 19103

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