

NASD NOTICE TO MEMBERS 93-1

SEC Approval of
Amendment to Article III,
Section 15 of the NASD®
Rules of Fair Practice;
Effective December 3,
1992

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The Securities and Exchange Commission (SEC) has approved an amendment to Article III, Section 15 of the NASD® Rules of Fair Practice. The amendment permits NASD members to use negative-response letters in bulk exchanges of money market mutual funds, provided the bulk exchanges are effected at net asset value and are limited to situations involving mergers and acquisitions of money market mutual funds, a change of clearing members, or an exchange of money market mutual funds used in sweep accounts. The amendment requires that the negative-response letter contain a tabular comparison of the nature and amount of fees charged by each fund as well as a comparative description of the investment objectives of each fund and a prospectus of the fund to be purchased. In addition, members cannot take action based on the negative-response letter until at least 30 days after the date the letter was mailed. The text of the amendment follows this Notice.

Background

To protect against abuse of discretion and overreaching, Article III, Section 15 of the NASD Rules of Fair Practice requires written authority from a customer before a member or a registered representative can exercise discretion in a customer's account. In *Notice to Members 91-39* (June 1991), the NASD reminded members that the use of negative-response letters may violate the provisions of Article III, Section 15. Negative-response letters permit the automatic execution of a recommendation, contained in such letters, to exchange mutual funds if a customer does not respond to the letter by a specific date. The violation

would occur if a member automatically executed an exchange without prior written authority from the customer permitting the member to exercise discretion in the account.

Following the distribution of *Notice to Members 91-39*, the NASD received requests from members to consider amending Article III, Section 15 to exempt the use of negative-response letters in bulk exchanges of money market mutual funds in certain situations involving mergers and acquisitions of such funds, a change of clearing members, and the exchange of money market mutual funds used in sweep accounts where investment performance is not the primary reason for the exchange.

The NASD recognized that it is often necessary to notify hundreds and, sometimes, several thousand money market mutual fund share-owners of an impending fund exchange. It may be an extremely difficult, if not impossible, administrative task to contact each non-replier and solicit approval of the fund exchange. At best, contacting individuals for approval results in considerable delays and added cost. The NASD determined that, by eliminating an obstacle to the efficient and timely execution of such bulk exchanges, where customers are at little or no risk, customers and NASD members would benefit.

Description of Amendment

Article III, Section 15 has been amended to permit an exemption for the use of negative-response letters in bulk exchanges of money market mutual funds provided the bulk exchanges are effected at net asset value and are limited to three situations. The first situation involves the use of a negative-response letter to effect the bulk

exchange of money market mutual funds resulting from the merger or acquisition of a currently used money market fund. The second situation involves the use of a negative-response letter to effect the bulk exchange of money market mutual funds necessitated by the member's change of its respective clearing member and the money market mutual fund that such clearing member utilizes. The third situation involves the use of a negative-response letter to effect the bulk exchange of money market mutual funds to enable a member to utilize a different fund from that which is being used currently as the investment vehicle for a sweep account. In such sweep accounts, a customer's credit balances are automatically invested in the sweep account for the benefit of the customer.

Four requirements apply to the availability of the negative-response letter exemption. The negative-response letter must include a tabular comparison of the nature and amount of fees charged by each fund. The negative-response letter must also include a comparative description of the investment objective of each fund.

A prospectus of the fund to be purchased must accompany the negative-response letter. The negative-response feature also cannot be activated until at least 30 days after the date the negative-response letter was mailed.

Effective Date

The amendment was approved by the SEC on December 3, 1992 and was immediately effective. Questions concerning this Notice may be directed to R. Clark Hooper at (202) 728-8329.

Amendment to Article III, Section 15 to the NASD Rules of Fair Practice

(**Note:** New language is underlined.)

Discretionary Accounts

Sec. 15

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Exceptions

(d)(1) This section shall not apply

to discretion as to the price at which or the time when an order given by a customer for the purchase or sale of a definite amount of a specified security shall be executed.

(d)(2) This section shall not apply to bulk exchanges at net asset value of money market mutual funds ("funds") utilizing negative response letters provided:

(i) The bulk exchange is limited to situations involving mergers and acquisitions of funds, changes of clearing members and exchanges of funds used in sweep accounts.

(ii) The negative response letter contains a tabular comparison of the nature and amount of the fees charged by each fund.

(iii) The negative response letter contains a comparative description of the investment objectives of each fund and a prospectus of the fund to be purchased.

(iv) The negative response feature will not be activated until at least 30 days after the date on which the letter was mailed.

NASD NOTICE TO MEMBERS 93-2

Market-Maker Obligations With Regard to Display of Size in Quotations

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training
-

Executive Summary

Since December 1, 1990, market makers in Nasdaq Small-Cap MarketSM securities that also make markets in the Small Order Execution System (SOESSM) have had to display size in their quotations of at least 500 shares. Effective February 1, 1993, this requirement will apply to all market makers in Nasdaq Small-Cap equity issues irrespective of their participation in SOES.

Background and Discussion

The Securities and Exchange Commission (SEC) has approved an amendment to Schedule D of the NASD[®] By-Laws requiring market makers in Nasdaq Small-Cap Market securities to display size in their quotations equal to the maximum order size in SOES, 500 shares.

In 1990, the SEC approved a rule proposal by the NASD to require mandatory display of size for market makers that participate in SOES¹ that included all market makers in Nasdaq National Market[®] securities and those market makers that voluntarily participated in SOES for Nasdaq Small-Cap stocks. The current rule proposal will extend that requirement to all market makers in Nasdaq Small-Cap issues, whether or not they participate in SOES.

Under the Rules of Practice and Procedures for SOES, market makers have to execute orders through SOES in sizes equal to or smaller than the "maximum order size" published from time to time by the NASD. These order-size limits are currently set at 200, 500, and 1,000 shares for Nasdaq National Market issues; and 500 shares for Nasdaq Small-Cap issues. The NASD

believes that it is now appropriate to expand the requirement to all market makers in Nasdaq Small-Cap securities because display of size in quotations reflects a more realistic picture of the actual size of executions available and the depth of the market in each security. In addition, display of size enhances investor knowledge and benefits issuers by publicizing the liquidity and depth of the market for their securities.

Additionally, requiring all Nasdaq[®] market makers to display minimum size in their quotations will end the inequitable application of the current display requirements. The requirement to post 500 shares now applies only to market makers that choose to participate in SOES, since SOES is voluntary for Nasdaq Small-Cap stocks. The market makers choosing to participate in SOES must also honor all incoming orders at their displayed size of 500 shares under the SEC's firm quote rule, Rule 11AC1-1. Thus, SOES market makers are disadvantaged by the current rule because they must honor phone orders from competing non-SOES market makers that need only execute orders for 100 shares in the same issues. The NASD believes that extending the requirement to display size to all market makers, whether they participate in SOES or not, is an equitable remedy.

Accordingly, the SEC has approved a rule requiring market makers in Nasdaq Small-Cap securities to display 500 shares in their quotation sizes. The NASD indicated that all Nasdaq Small-Cap securities will be subject to the 500-share size requirements unless the security has a bid price of \$10 or more and an average daily non-block volume of less than 1,000 shares. In the

¹See Release 34-28450 (Sept. 18, 1990).

Nasdaq Small-Cap issues that fall under these thresholds, market makers will continue to be required to post size of a normal unit of trading, 100 shares. Nasdaq convertible debt securities will also be exempt from the new size-display requirements. The NASD will periodically (approximately every six months) review and analyze the trading characteristics of Nasdaq Small-Cap securities, including share price and average volume in the stock, to determine whether any modifications to the 500-share requirement are appropriate and will publish a *Notice to Members* regarding any modifications.

Questions concerning this Notice may be directed to Beth E. Weimer, Associate General Counsel, at (202) 728-6998.

(**Note:** New language is underlined.)

Schedule D

Part VI

Requirements Applicable to Nasdaq Market Makers

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Sec. 2 Character of Quotations

(a) Two-sided Quotations. For each security in which a member is registered as a market maker, the member shall be willing to buy and sell such security for its own account on a continuous basis and shall enter and maintain two-sided quotations

in the Nasdaq System, subject to the procedures for excused withdrawal set forth in Section 8 below. Each member registered as a Nasdaq market maker [and as a market maker in the Small Order Execution System] shall display the size for each quotation which size shall be no less than the maximum order size for such security eligible for execution through the Small Order Execution System, as shall be published from time to time by the Association pursuant to paragraph (a)(7) of the Rules of Practice and Procedure for the Small Order Execution System. Maximum order sizes for Nasdaq/NMS securities shall be 200, 500, or 1,000 shares depending upon trading characteristics of the securities. Maximum order size for Nasdaq Small-Cap securities shall be 100 or 500 shares depending upon trading characteristics of the securities. A 500 share display size for Nasdaq Small-Cap securities shall apply to securities with an average daily non-block volume of 1,000 shares or more and a bid price of less than \$10.00 per share. A 100 share display size for Nasdaq Small-Cap securities shall apply to securities with an average daily non-block volume of less than 1,000 shares a day and a bid price equal to or greater than \$10.00 a share. Individual securities may be reclassified from time to time depending upon unique circumstances as determined by the Association. These sizes shall not be applicable to convertible debt securities listed in Nasdaq.

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Rules of Practice and Procedures for the Small Order Execution System

(a) Definitions

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7. The term "maximum order size" shall mean the maximum size of individual orders for a security that may be entered into or executed through SOES. The maximum order size for each security shall be published from time to time by the Association. In establishing the maximum order size for each Nasdaq/NMS security, the Association will give consideration to the average daily non-block volume, bid price, and number of market makers for each security.

Maximum order sizes for Nasdaq/NMS securities shall be 200, 500, or 1,000 shares depending upon trading characteristics of the securities. Maximum order size for Nasdaq Small-Cap securities shall be 500 shares. These sizes may be adjusted on an issue by issue basis, depending upon unique characteristics of the issue as determined by the Association.

NASD NOTICE TO MEMBERS 93-3

SEC Approval of Amendments to Branch-Office Fees

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
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- Trading
- Training

Executive Summary

The Securities and Exchange Commission (SEC) has approved an amendment to Schedule A of the NASD[®] By-Laws that permits the NASD to assess a \$50 fee for the registration of each branch office and an annual \$50 fee based on the number of registered branch offices or the number of registered persons associated with the member, whichever is lower. Previously, the number of registered persons was not considered in calculating the annual fee. The new provisions apply to assessments on member firms for the calendar year ended December 31, 1992. The text of the amendment follows this Notice.

Background and Discussion

The SEC has approved an amendment to Schedule A, Section 2 of the NASD By-Laws that permits the NASD to assess a \$50 fee for the registration of each branch office and an annual \$50 fee based on the number of registered branch offices or the number of registered persons associated with the member, whichever is lower.

NASD members were previously required to pay an annual fee for each registered branch office. The fee was assessed on registration of the branch and annually thereafter. The fee was imposed for each location of a member that met the definition of "branch office," as defined in Section 27 of the NASD Rules of Fair Practice, and was registered with the NASD. Section 27(g)(2) defines "branch office" as any location where a member conducts an investment banking or securities business. In addition, Section 27(g) provides that a branch office is any location where a member performs any function of an Office of Supervisory Jurisdiction (OSJ);

publicly displays signage; operates from public areas of buildings, such as bank branches, even when such locations are temporarily staffed; or advertises an address in any public media. (See *Notice to Members 92-18* April 1992.)

The reason for the amendment is the NASD concern with the inequity that could result from imposing branch-office fees on a member with a disproportionately large number of branch-office locations relative to its size and number of registered representatives and principals. A member with many offices staffed by registered persons on a part-time, rotating basis could be assessed a disproportionately large branch-office fee. To eliminate possible inequities, the NASD decided to revise the branch-office fee structure.

The amendment to Section 2 clarifies that a \$50 fee is imposed for registering each branch office and that each branch office is also subject to a \$50 annual fee. The amendment provides that the annual fee is calculated at year-end based on either the number of the registered branch offices or the number of registered representatives and principals at that time. Thus, where the number of a member's registered branch offices exceeds the combined number of the member's registered persons, the member will not be assessed branch-office renewal fees on the difference between the two. Even if the annual fee is based on the member's registered persons, members must still register each location that meets the definition of a branch office. The amendments apply to assessments on member firms for the calendar year that ended December 31, 1992.

Implementation

To take advantage of the new fee assessment structure, members need to review their operations to determine which locations must be registered with the NASD because they meet the definition of "branch office" in Section 27. Members should use Schedule E to Form BD to register any unregistered locations and to identify all locations as full- or part-time. The NASD must receive any updates to Schedule E **by March 15, 1993**, to affect the member's assessment for calendar year 1992. Members may file Schedule E to Form BD either in hard-copy form with the NASD's Central Registration Depository (CRD) or electronically through the Firm Access Query System (FAQS) if the members are subscribers. Call the FAQS hotline at (301) 590-6862 or the Member Services Phone Center at (301) 590-6500 for details

on FAQS. For questions related to the filing of Schedule E to Form BD for the registration of branch offices, call the Member Services Phone Center.

Questions regarding this Notice should be directed to John F. Vaughn, Assistant Director, Membership at (301) 590-6500, or Elliott R. Curzon, Senior Attorney, Office of General Counsel, at (202) 728-8451.

Text of Amendment to Schedule A to the NASD By-Laws

(Note: New text is underlined; deleted text is in brackets.)

Section 2 — Fees

(a) Each member shall be assessed a fee of \$50 for the registration of each [registered] branch office, as defined in the By-Laws[.]. Each

member shall be assessed an annual fee for each branch office [which is open during any part of the Association's fiscal year.] in an amount equal to the lesser of (1) \$50 per registered branch, or (2) the product of \$50 and the number of registered representatives and registered principals associated with the member at the end of the Association's fiscal year.

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NASD NOTICE TO MEMBERS 93-4

1993 Renewal Rosters And Final Adjusted Invoices

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
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- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The 1992-93 NASD® broker/dealer and agent registration renewal cycle begins its second phase this month. The NASD is publishing information in this Notice to assist members in reviewing, reconciling, and responding to the Final Adjusted Invoice packages that were mailed to all member firms in mid-January.

Final Adjusted Invoice Packages

On or about January 13, 1993, the NASD mailed final adjusted invoices and renewal rosters to all NASD member firms. The invoice reflects year-end 1992 total fees for NASD personnel assessments; NASD branch-office assessments; New York Stock Exchange (NYSE), American Stock Exchange (ASE), Chicago Board Options Exchange (CBOE), and Pacific Stock Exchange (PSE) maintenance fees; state agent renewal fees; and state broker/dealer renewal fees. It also reflects payment submitted by an NASD member in response to the initial renewal invoice mailed in November 1992.

The final invoice includes a renewal roster that lists each firm's NASD and, if applicable, NYSE-, ASE-, CBOE-, and PSE-registered personnel as of year-end 1992. In addition, the roster lists alphabetically all firm agents whose registrations were renewed in states. Firms with registered branch offices that were active as of December 31, 1992, will receive a branch-office roster in addition to the agent roster.

A member's final invoice shows an "amount due," a "credit due," or a "zero balance due." If a firm's year-end 1992 total of NASD, NYSE, ASE, CBOE, PSE, and state renewal fees exceeded the firm's payment submitted in response to the initial

renewal invoice, the NASD paid the additional renewal fees due at year-end on behalf of the member and will mail an "amount due" invoice to collect that sum.

If your invoice shows an amount due, please submit payment in the form of a check made payable to the National Association of Securities Dealers, Inc. The check should be drawn on the member firm's bank account, with the firm's Central Registration Depository (CRD) number included on the check. Submit the check along with the top portion of the invoice and mail it in the return envelope provided. **Payments must be received by the NASD no later than March 12, 1993.**

If the firm's payment submitted in response to the initial renewal invoice exceeded its year-end 1992 total of NASD, NYSE, ASE, CBOE, PSE, and state renewal fees, a "credit due" invoice was issued. If your firm's invoice shows a credit due of \$100.00 or more and you would like it paid to your firm, please detach and sign the top portion of the invoice and send it to Wendy L. Cook, Special Services, NASD, Inc., 9513 Key West Avenue, Rockville, Maryland 20850. This invoice stub must be signed by an officer or principal of your firm. In addition, please note somewhere on your invoice stub the name and address of the firm's contact to whom the NASD should send the check. Refund checks will be mailed to members within three weeks of the date the NASD receives a signed invoice stub. If the NASD does not receive a check refund request **by March 12, 1993**, the credit amount will be applied to your firm's CRD account. Amounts under \$100.00 will be automatically credited to your firm's CRD account during the week of March 15, 1993.

A final adjusted invoice with a zero balance requires no further action by the member.

Reviewing the Renewal Roster

Member renewal rosters include all agent registrations renewed for 1993. **Since registrations pending approval or deficient at year-end 1992 were not assessed renewal fees, those registrations are not reported on the renewal roster.** Members should examine their rosters carefully to ensure that all

registration approvals and terminations are reflected properly.

If discrepancies exist, report them **in writing** along with supporting documentation, such as Notices of Approval/Termination, Forms U-4 or U-5, or Schedule E amendments. Report the discrepancies directly to the NASD, NYSE, ASE, CBOE, PSE, or the applicable state. **All renewal roster discrepancies must be reported by March 19, 1993.**

The inside cover of the renewal roster contains detailed instructions

to assist members in completing the renewal process.

On or about January 5, 1993, the South Dakota Division of Securities moved to 118 W. Capitol, Pierre, South Dakota 57501-5070. The address listed on the back cover of your firm's renewal roster is incorrect.

Questions regarding this Notice may be directed to NASD Member Services Phone Center at (301) 590-6500.

NASD NOTICE TO MEMBERS 93-5

The NASD® published the following *Notices to Members* during 1992. Duplicate copies are available at \$25 per monthly or special issue. A bound-volume, indexed reprint of the entire year's Notices is also available at \$150. Requests, accompanied by a self-addressed mailing label and a check payable to the National Association of Securities Dealers, Inc., or credit card information, should be sent to NASD MediaSource, SM P.O. Box 9403, Gaithersburg, MD 20898-9403. Credit card telephone orders for bound volumes can be made by telephoning (301) 590-6578, Monday to Friday, 9 a.m. to 5 p.m., Eastern Time.

Annual Check List of NASD *Notices to Members*

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- Senior Management
- Corporate Finance
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NASD NOTICE TO MEMBERS 93-6

Presidents' Day — Trade Date-Settlement Date Schedule

Suggested Routing

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- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
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Securities exchanges and The Nasdaq Stock MarketSM will be closed on Monday, February 15, 1993, in observance of Presidents' Day. "Regular way" transactions made on the preceding business days will be subject to the settlement date schedule listed below.

Trade Date	Settlement Date	Reg. T Date*
Feb. 5	12	17
8	16	18
9	17	19
10	18	22
11	19	23
12	22	24
15	Markets Closed	—
16	23	25

Brokers, dealers, and municipal securities dealers should use these settlement dates to clear and settle transactions pursuant to the NASD[®] Uniform Practice Code and Municipal Securities Rulemaking Board Rule G-12 on Uniform Practice.

Questions regarding the application of these settlement dates to a particular situation may be directed to the NASD Uniform Practice Department at (212) 858-4341.

*Pursuant to Sections 220.8(b)(1) and (4) of Regulation T of the Federal Reserve Board, a broker/dealer must promptly cancel or otherwise liquidate a customer purchase transaction in a cash account if full payment is not received within seven (7) business days of the date of purchase or, pursuant to Section 220.8(d)(1), make application to extend the time period specified. The date by which members must take such action is shown in the column entitled "Reg. T Date."

NASD NOTICE TO MEMBERS 93-7

Nasdaq National Market
Additions, Changes,
And Deletions As of
December 21, 1992

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

As of December 21, 1992, the following 47 issues joined the Nasdaq National Market,[®] bringing the total number of issues to 2,977:

Symbol	Company	Date	SOES Execution Level
AMEP	American Educational Products Inc.	11/23/92	1000
CRTQZ	Cortech Inc.	11/24/92	1000
FORBP	Fortune Bancorp, Inc. Ser A 8% Conv Pfd	11/24/92	1000
HSRS	HS Resources, Inc.	11/24/92	1000
NWTH	NetWorth, Inc.	11/25/92	200
BKUNA	BankUnited, A Savings Bank Cl A	12/1/92	200
MAYF	Mayflower Group, Inc.	12/1/92	500
MMTCY	Memtec Limited ADRs	12/1/92	1000
AACE	Ace Cash Express, Inc.	12/2/92	1000
MIHO	Miles Homes, Inc.	12/3/92	1000
PHBKR	Peoples Heritage Fin. Group, Inc. Rts 12/31/92	12/4/92	1000
EDUSF	EduSoft Ltd. - Ordinary Shares	12/8/92	1000
SALD	Fresh Choice, Inc.	12/9/92	1000
INFB	InterFirst Bankcorp, Inc.	12/9/92	200
ACXTV	ACX Technologies, Inc.	12/10/92	1000
MWHS	Micro Warehouse, Inc.	12/10/92	1000
OLYM	Olympic Financial Ltd.	12/10/92	1000
HGGR	Haggar Corp.	12/11/92	1000
MDLD	Midland Financial Group, Inc.	12/11/92	1000
PREZ	President Riverboat Casinos, Inc.	12/11/92	1000
UWST	United Waste Systems, Inc.	12/11/92	1000
AUFN	AutoFinance Group, Inc.	12/14/92	200
HYALF	Hyal Pharmaceutical Corporation	12/14/92	1000
KEND	Kendall International, Inc.	12/14/92	1000
DEPCA	DEP Corporation Cl A	12/15/92	1000
NUHC	Nu Horizons Electronics Corp.	12/15/92	500
PFIL	Purolator Products Company	12/15/92	1000
RSCR	Res-Care, Inc.	12/15/92	1000
SNPL	Snapple Beverage Corp.	12/15/92	1000
VSCI	Vision-Sciences, Inc.	12/15/92	1000
FLWR	Celebrity, Inc.	12/16/92	1000
CPWR	Compuware Corporation	12/16/92	1000
MCBX	MB Communications, Inc.	12/16/92	500
MARY	St. Mary Land & Exploration Company	12/16/92	1000
SYRA	Syratech Corporation	12/16/92	500
TRID	Trident Microsystems, Inc.	12/16/92	1000
DANKY	Danka Business Systems PLC ADRs	12/17/92	500
EVTC	Environmental Technologies Corp.	12/17/92	200
EVTCW	Environmental Technologies Corp. Wts 12/1/97	12/17/92	200

Symbol	Company	Date	SOES Execution Level
SISGF	ISG International Software Group Ltd. - Ord Shares	12/17/92	1000
CKOR	SEACOR Holdings, Inc.	12/17/92	1000
BPIEW	BPI Environmental, Inc. Wts Cl A 12/6/94	12/18/92	1000
BPIEZ	BPI Environmental, Inc. Wts Cl B 10/7/96	12/18/92	1000
CBMI	Creative Bio-Molecules, Inc.	12/18/92	1000
EXTR	Exstar Financial Corp.	12/18/92	1000
GBCT	GBC Technologies, Inc.	12/18/92	1000
HMSY	Health Management Systems, Inc.	12/18/92	1000

Nasdaq National Market Symbol and/or Name Changes

The following changes to the list of Nasdaq National Market securities occurred since November 21, 1992:

New/Old Symbol	New/Old Security	Date of Change
PMDX/CCFR	Primedex Health Systems Inc./CCC Franchising Corp.	11/24/92
ASKI/ASKI	The ASK Group, Inc./ASK Computer Systems Inc.	11/27/92
INSUA/INSUA	Insituform Technologies, Inc. Cl A/Insituform of North America, Inc. Cl A	12/10/92
ALPC/HINS	Allmerica Property & Casualty Companies, Inc./Hanover Insurance Co.	12/14/92
DEPCB/DEPC	DEP Corporation - Cl B/DEP Corporation	12/15/92
MDCOR/	Marine Drilling Companies, Inc. Rts 12-23-92/ Marine Drilling Companies, Inc. Rts 12-11-92	12/15/92
UCFC/UNCF	United Companies Financial Corporation/ United Companies Financial Corporation	12/15/92
IPPIF/IPPIF	Interprovincial Pipe Line System Inc./Interprovincial Pipe Line Inc.	12/18/92

Nasdaq National Market Deletions

Symbol	Security	Date
FLGF	Flagship Financial Corp.	11/23/92
ILIO	Ilio, Inc.	11/24/92
RMUC	Rocky Mount Undergarment Co., Inc.	11/24/92
HLTH	Healthsource, Inc.	12/2/92
UNMAA	Uni-Marts Inc. Cl A	12/2/92
ATEL	Advanced Telecommunications Corp.	12/7/92
BANQ	Burritt InterFinancial	12/7/92
CNCRE	Cencor, Inc.	12/7/92
SNLB	Second National Bancorporation	12/7/92
SSLN	Security Investments Group, Inc.	12/7/92
FFBK	First Florida Banks, Inc.	12/8/92
TEJS	Tejas Gas Corporation	12/9/92
CSTLR	Constellation Bancorp Rts 12/10/92	12/10/92
IGLSF	Insituform Group, Ltd.	12/10/92
CKSB	CK Federal Savings Bank	12/14/92
EAFC	Eastland Financial Corp.	12/14/92

Symbol	Security	Date
MTOR	Meritor Savings Bank	12/14/92
PTLX	Patlex Corporation	12/14/92
SNRU	Sunair Electronics, Inc.	12/14/92
BETZ	Betz Laboratories, Inc.	12/15/92
HFET	Home Financial Corp.	12/15/92
SBRNW	SANBORN Inc. Wts 8/7/96	12/15/92
SBRNP	SANBORN Inc. Pfd A	12/15/92
BRDN	Brandon Systems Corporation	12/16/92
CUSA	CompuUSA Inc.	12/17/92
ABDN	American Biodyne, Inc.	12/21/92
FLSPC	FLS Holdings Inc. Series A Pfd	12/21/92
WECA	Western Capital Investment Corp.	12/21/92
AESM	Aero Systems, Inc.	12/22/92
PHBKR	Peoples Heritage Financial Gropu Inc. Rts	12/22/92
SMBX	Symbolics, Inc.	12/22/92

Questions regarding this Notice should be directed to Mark A. Esposito, Supervisor, Market Listing Qualifications, at (202) 728-8002.

Questions pertaining to trade reporting rules should be directed to Bernard Thompson, Assistant Director, NASD Market Surveillance, at (301) 590-6436.

NASD DISCIPLINARY ACTIONS

Disciplinary Actions Reported for January

The NASD® is taking disciplinary actions against the following firms and individuals for violations of the NASD Rules of Fair Practice; securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board. Unless otherwise indicated, suspensions will begin with the opening of business on Monday, January 18, 1993. The information relating to matters contained in this Notice is current as of the fifth of this month. Information received subsequent to the fifth is not reflected in this publication.

Firms Expelled

Hasan Growney Company, Inc. (New York, New York) was expelled from membership in the NASD for failing to pay a \$10,000 arbitration award. In a separate action, the firm was also expelled for failure to pay a \$368.75 arbitration award.

Firms Suspended

Equitrade, Inc. (Nashville, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which the firm was fined \$5,000 and suspended from membership in the NASD for six months. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it engaged in a securities business without maintaining its required minimum net capital and failed to prepare an accurate computation of its net capital. In addition, the NASD determined that the firm failed to give immediate telegraphic notice to the NASD of its failure to comply with the minimum net capital requirements.

Firms Suspended, Individuals Sanctioned

First Choice Securities Corporation (Englewood, Colorado) and **Gregory F. Walsh (Registered Principal, Los Angeles, California)** were fined \$20,000, jointly and severally. In addition, the firm was suspended from membership in the NASD for 60 days and required to immediately comply with all provisions of the firm's restriction agreement.

The National Business Conduct Committee (NBCC) imposed the sanctions following an appeal of a decision by the District Business Conduct Committee (DBCC) for District 3. The sanctions were based on findings that the firm, acting through Walsh, opened four branch offices in violation of the terms of its restriction agreement with the NASD. Specifically, the firm, acting through Walsh, made markets in 15 securities and maintained a larger inventory than the agreement allowed.

Osborne, Stern & Company, Inc. (Los Angeles, California) and **Douglas W. Osborne, Sr. (Registered Principal, Venice, California)** were fined \$270,454, jointly and severally. The firm was suspended from operating as a broker/dealer for 90 days, and Douglas Osborne was suspended from association with any NASD member in any capacity for 90 days. The Securities and Exchange Commission (SEC) affirmed the sanctions following an appeal of a November 1990 NBCC decision.

The sanctions were based on findings that the firm, acting through Osborne, charged retail customers unfair prices in contravention of the Board of Governors' Interpretation with respect to the NASD Mark-Up Policy. The fraudulently excessive

markups ranged from 32.58 to 191.67 percent above the firm's contemporaneous cost. In addition, the firm violated its restrictive agreement with the NASD when it traded for its own account by effecting numerous principal transactions.

Firms Fined, Individuals Sanctioned

Escalator Securities, Inc. (Palm Harbor, Florida) and Howard A. Scala (Registered Principal, Tarpon Springs, Florida) were fined \$50,000, jointly and severally. In addition, Scala was suspended from association with any NASD member in any capacity for one month and required to requalify by examination before acting in a registered capacity.

The NBCC imposed the sanctions following an appeal of a decision by the DBCC for District 9. The sanctions were based on findings that the firm, acting through Scala, effected principal sales of a non-Nasdaq, non-exchange security to public customers at unfair prices, including markups ranging from 68.2 to 147.5 percent above the firm's contemporaneous costs.

Furthermore, the firm, acting through Scala, charged its customers \$33 per transaction in addition to the price of the securities disclosed in the prospectuses. In addition the firm, acting through Scala, effected options transactions for public customers while failing to obtain required option account information. Also, the firm failed to execute two mutual fund subscriptions promptly.

First Choice Securities Corp. (Englewood, Colorado) and Sheldon Owen Fertman (Registered Principal, Denver, Colorado) were fined \$10,000,

jointly and severally and Fertman was barred from association with any NASD member in any principal capacity. The NBCC imposed the sanctions following an appeal of a decision by the DBCC for District 3. The sanctions were based on findings that the firm and Fertman allowed and assisted an unregistered individual to conduct securities transactions through the firm.

Firms Fined

Century Capital Corp. of South Carolina (Greenville, South Carolina) was fined \$10,000. The SEC affirmed the sanction following an appeal of a December 1990 NBCC decision. The sanction was based on findings that, in contravention of the NASD's Mark-Up Policy, the firm charged its customers unfair prices in the sales of five securities.

This action has been appealed to a United States Circuit Court of Appeals, and the sanction is not in effect pending consideration of the appeal.

Kessler Asher Clearing, Inc. (Chicago, Illinois) submitted a Letter of Acceptance, Waiver and Consent pursuant to which the firm was fined \$2,000, jointly and severally with a registered representative, and fined an additional \$10,625, separately. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that the firm violated the Board of Governors' Free-Riding and Withholding Interpretation by selling shares of a new issue that traded at a premium in the immediate aftermarket to a restricted account.

Firms and Individuals Fined

American Business Securities, Inc. (Irvine, California) and Barry John Zimmermann (Registered Principal, Costa Mesa, California) submitted a Letter of Acceptance, Waiver and Consent pursuant to which the firm and Zimmermann were fined \$10,000, jointly and severally. In addition, the firm was fined \$7,500, jointly and severally with another registered principal.

Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Zimmermann, participated in six contingent offerings of securities and represented to investors that a certain number of units would be sold by a designated closing date before investors' funds would be released to the issuer. However, the NASD determined that the investors' funds were withdrawn from separate bank escrow accounts before funds equal to, or in excess of, the specified level of sales cleared the banking system.

F.J. Garber & Co. (Sioux City, Iowa) and Frederick J. Garber (Registered Principal, Sioux City, Iowa) submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were fined \$10,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Garber, conducted a securities business while failing to maintain its required minimum net capital.

Paulson Investment Company, Inc. (Portland, Oregon), Chester Leon Frederick Paulson (Registered Principal, Portland, Oregon), Thomas Elroy

McChesney (Registered Principal, Gladstone, Oregon), and Richard Arthur Boege (Registered Principal, Portland, Oregon) submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were fined \$60,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanction and to the entry of findings that the firm, acting through Paulson and McChesney, held itself out as a market maker for a common stock in the National Quotation Bureau, Inc., "Pink Sheets" and the OTC Bulletin Board,[®] and acted as a market maker in the security while participating in an apparent distribution of its common stock in violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-6 thereunder.

The findings also stated that, in contravention of the Board of Governors' Free-Riding and Withholding Interpretation, the firm, acting through McChesney, sold shares of a new issue that traded at a premium in the immediate aftermarket to restricted accounts. In connection with this sale, the NASD also found that the firm, acting through McChesney, submitted an inaccurate free-riding questionnaire to the NASD.

Furthermore, the findings stated that the firm, acting through Boege, failed to establish, maintain, or enforce written supervisory procedures or otherwise to supervise adequately certain sales activities in the firm including compliance with the Board of Governors' Interpretation with respect to Free-Riding and Withholding. Moreover, the NASD determined that the firm, acting through Boege, failed to conduct an annual branch audit for 20 branch offices of which 7 were offices of supervisory jurisdiction

pursuant to the firm's own supervisory procedures, and failed to conduct an annual compliance meeting for its registered representatives in those 20 offices.

Individuals Barred or Suspended

Lori Ann Anderson (Registered Representative, Logan, Utah) was fined \$108,072 and barred from association with any NASD member in any capacity. The fine may be reduced by restitution made to a member firm or to clients involved. The sanctions were based on findings that after obtaining 21 checks totaling \$58,072.51 and made payable to 19 insurance customers, Anderson forged the customers' endorsements on the checks and converted the proceeds to her own use and benefit. Moreover, to obtain the aforementioned checks, Anderson changed the addresses on 11 of these customers' accounts to an address she controlled. In addition, Anderson sent false and misleading information to insurance customers regarding their accounts.

Brian Thayer Baker (Registered Representative, St. Louis, Missouri) was fined \$26,700 and suspended from association with any NASD member in any capacity for 30 days. The sanctions were based on findings that, in contravention of the Policy of the Board of Governors concerning Fair Dealing with Customers, Baker executed unauthorized securities transactions in the account of a public customer's account.

Michael A. Bakonyi (Registered Representative, Fairfield, Ohio) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$70,000, barred from association with any member of the NASD in any capacity, and must pay \$10,340.25 in restitution

to his member firm. Without admitting or denying the allegations, Bakonyi consented to the described sanctions and to the entry of findings that he misappropriated and converted to his own use customer funds totaling \$10,340.82 which were designated for insurance premium payments. In addition, Bakonyi failed to respond to NASD requests for information.

Richard Barnett (Registered Representative, Bronx, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 15 business days.

Without admitting or denying the allegations, Barnett consented to the described sanctions and to the entry of findings that he recommended to three public customers the purchase of securities based on price predictions and other misrepresentations. Based on this information, the NASD found that the customers purchased the stock. According to the findings, Barnett's subsequent failure to enter a stop order as promised for one of the three customers resulted in significant losses for that customer.

Robert Billings (Registered Representative, Sheboygan, Wisconsin) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$200,000, barred from association with any NASD member in any capacity, and required to pay \$169,648.64 in restitution. Without admitting or denying the allegations, Billings consented to the described sanctions and to the entry of findings that he obtained \$214,067.98 in insurance policy premiums from nine insurance customers. The NASD found that Billings failed to follow the cus-

tomers' instructions and used \$169,648.64 of those funds for other purposes. Billings also failed to respond to NASD requests for information.

Raymond E. Blitstein (Registered Representative, Denver, Colorado) was fined \$5,000 and barred from association with any NASD member in all capacities. The NBCC imposed the sanctions following an appeal of a decision by the DBCC for District 3. The sanctions were based on findings that Blitstein failed to pay a \$9,100 NASD arbitration award.

Mark Victor Booth (Registered Representative, Minneapolis, Minnesota) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Booth failed to respond to NASD requests for information concerning his termination from a member firm.

Robert M. Celeste (Registered Representative, Kennebunkport, Maine) was fined \$10,000 and suspended from association with any NASD member in any capacity for six months. The sanctions were based on findings that Celeste recommended and caused the execution of an investment that was unsuitable for a public customer. In connection with this transaction, Celeste also engaged in a private securities transaction without providing prior written notification to his member firms.

Ray T. Clancy (Registered Representative, Godfrey, Illinois) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$75,000, barred from association with any NASD member in any capacity, and required to pay \$33,000 in restitution.

Without admitting or denying the allegations, Clancy consented to the described sanctions and to the entry of findings that without his customers' knowledge or consent Clancy requested the withdrawal of dividends totaling \$33,000 from their insurance policies and had the proceed checks sent to a post office box that was not the address of record for any of the customers. Furthermore, the NASD determined that Clancy endorsed the checks and used the proceeds for purposes other than to benefit the customers. The findings also stated that Clancy failed to respond to NASD requests for information.

Kevin R. Curtis (Registered Principal, Dallas, Texas) and **Catherine W. Yox (Registered Principal, Tulsa, Oklahoma)** submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were fined \$7,500, jointly and severally. In addition, Curtis was suspended from association with any NASD member in any capacity for two weeks and required to requalify by examination as a direct participation programs principal. Yox was also suspended from association with any NASD member in any capacity for one week. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that, in joint venture offerings, a member firm, acting through Curtis and Yox, failed to keep current books and records and violated various provisions of Regulation D of the Securities Act of 1933.

The NASD also found that the same firm, acting through Curtis, prepared inaccurate net capital computations and conducted a securities business without maintaining its required minimum net capital. In addition, the NASD determined that the firm, acting

through Curtis, failed to handle customer escrowed funds properly and participated in three programs without disclosing a definite termination date to meet the contingency. Furthermore, the findings stated that the firm, acting through Curtis, accepted a subscription document for a joint venture from a public customer without having reasonable grounds for believing that the investment was suitable for the customer. Also according to the findings, Curtis, acting on behalf of the firm, failed to make appropriate disclosures of certain third-party ownership of a material interest in the offering memoranda for two joint ventures. The findings also stated that the firm, acting through Curtis, failed to evidence supervisory approval on subscription documents or any other document used in transactions with certain public customers in joint ventures. The NASD also found that the firm, acting through Curtis, prepared and submitted inaccurate quarterly FOCUS Part IIA reports.

The NASD further determined that the firm, acting through Yox, conducted a securities business while maintaining less than the minimum net capital and failed to file timely FOCUS Part IIA reports. The findings stated that Yox, acting for the firm, also failed to prepare and maintain written supervisory procedures and to prepare and maintain fingerprint records for the director and a stockholder of the firm. According to the findings, the firm, acting through Yox, failed to maintain fidelity bond coverage and to ensure that the firm's president was qualified as principal.

Robert D. Cutchall (Registered Representative, Oklahoma City, Oklahoma) was fined \$30,000 and barred from association with any NASD member in any capacity. The sanctions were based on find-

ings that Cutchall induced a public customer to purchase stock by providing him with a written guarantee regarding a limited loss on an investment. In addition, Cutchall failed to respond to NASD requests for information.

Robert A. Eames (Registered Representative, West Jordan, Utah) and David M. Eames (Associated Person, Salt Lake City, Utah) were each fined \$70,000 and barred from association with any NASD member in any capacity. In addition, they were fined \$74,454, jointly and severally; however, the fine may be reduced by any restitution made either to customers or to any organization that reimbursed any of these customers.

The sanctions were based on findings that Robert and David Eames obtained from public customers 31 checks totaling \$74,453.75 to purchase securities. The respondents failed to purchase the intended securities and, instead, deposited the funds to a bank account. In addition, they failed to respond to NASD requests for information.

Robert Stephen Ellis (Registered Representative, Sylvan Lake, Michigan) was suspended from association with any NASD member in any capacity for five business days. The sanction was based on findings that Ellis failed to pay a \$7,025 NASD arbitration award in a timely manner.

Mark M. Ferguson (Registered Representative, Metairie, Louisiana) was fined \$85,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Ferguson received from a public customer a \$42,500 check for investment purposes, endorsed the check, and converted the funds

to his own use and benefit without the customer's knowledge or consent. In addition, Ferguson failed to respond to NASD requests for information.

David Joseph Fingerhut (Registered Representative, St. Louis, Missouri) submitted an Offer of Settlement pursuant to which he was fined \$2,500 and suspended from association with any NASD member in any capacity for six months. Without admitting or denying the allegations, Fingerhut consented to the described sanctions and to the entry of findings that he failed to disclose on a Uniform Application for Securities Industry Registration (Form U-4) that he had entered into a preliminary agreement with the Missouri Bar Committee to voluntarily surrender his license to practice law and accept a disbarment.

Samuel H. Galantz (Registered Representative, New York, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$6,500, required to pay \$13,968.75 in restitution to public customers, and suspended from association with any NASD member in any capacity for 10 business days.

Without admitting or denying the allegations, Galantz consented to the described sanctions and to the entry of findings that, in purchasing and selling securities for public customers, Galantz effected these transactions at unfair and unreasonable prices. The excessive gross sales credit charges ranged from 14.3 to 21.4 percent of the total cost to the customers for the transaction. Furthermore, the findings stated that certain of the aforementioned purchase and sale transactions were unsuitable for the customers.

Peter Paul E. Gepuela (Registered Representative, Glendale Heights, Illinois) was fined \$21,500, barred from association with any NASD member in any capacity, and required to pay \$1,476.23 in restitution to his member firm. The sanctions were based on findings that Gepuela obtained a \$1,476.23 check made payable to an insurance customer. These funds represented a surrender of the customer's insurance policy. Gepuela failed to forward the check to the customer and, instead, used the funds for purposes other than for the benefit of the customer. Gepuela also failed to respond to NASD requests for information.

David A. Gingras (Registered Representative, Wallingford, Pennsylvania) was fined \$45,000 and suspended from association with any NASD member in any capacity for six months. The SEC affirmed the sanctions following an appeal of a November 1990 NBCC decision. The sanctions were based on findings that Gingras executed transactions in two customer accounts that were speculative and excessive without having reasonable grounds for believing that the transactions were suitable considering the customers' financial situations and investment objectives. These transactions generated \$33,083 in commissions to Gingras and in \$140,404 losses to the two customers. Gingras also issued a guarantee against loss to one of these customers concerning the value of her account.

James Carroll Hale (Registered Principal, Richardson, Texas) was fined \$15,000, suspended from association with any NASD member in any capacity for 30 days, and suspended in any principal capacity until he requalifies as a principal. The sanctions were based on findings that a former member firm,

acting through Hale, effected transactions in securities while failing to maintain its required minimum net capital. In addition, in violation of the NASD's Mark-Up Policy, the firm, acting through Hale, effected principal sales with retail customers at unfair and unreasonable prices.

Toby Lynn Hickman (Registered Representative, Columbus, Ohio) was fined \$15,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Hickman received from four insurance customers \$236.44 for payment of insurance premiums and, instead, used the funds to pay premiums on other customers' insurance policies. In addition, Hickman failed to respond to NASD requests for information.

Peter Thompson Higgins (Registered Principal, Metuchen, New Jersey) was suspended from association with any NASD member in any capacity for three business days. The NBCC imposed the sanction following an appeal of a decision by the DBCC for District 10. The sanction was based on findings that Higgins failed to pay a \$13,015.63 arbitration award in a timely manner.

Higgins appealed this action to the SEC, and the sanction is not in effect pending consideration of the appeal.

Stewart E. Holzkenner (Registered Representative, New York, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$9,645, required to pay \$5,274.68 to customers, and to requalify as a general securities representative. In addition, he was suspended from association with any NASD member in any capacity for five business days.

Without admitting or denying the allegations, Holzkenner consented to the described sanctions and to the entry of findings that he executed, for three public customers, transactions with gross sales credits exceeding 5 percent of the total cost of the securities to the customers. The findings also stated that Holzkenner engaged in unsuitable transactions with two public customers. Furthermore, the NASD found that, in a sale to a public customer, Holzkenner incorrectly informed the customer that Holzkenner's member firm acted in an agency capacity when it had acted in a principal capacity, thereby giving the customer incorrect information as to Holzkenner's total remuneration for the trade.

Jack J. Illare (Registered Representative, Brooklyn, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$1,587.50, required to pay \$1,587.50 in restitution to public customers, and suspended from association with any NASD member in any capacity for three business days. Without admitting or denying the allegations, Illare consented to the described sanctions and to the entry of findings that he executed transactions for public customers and charged them excessive sales credits ranging from 15 to 23 percent of the total cost for the transaction.

John P. Karekos (Registered Principal, Fairport, New York) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Karekos consented to the described sanctions and to the entry of findings that he failed to follow a public customer's instructions to open an

Individual Retirement Account (IRA). In addition, the NASD determined that Karekos recommended to the same customer the purchase and sale of securities that were unsuitable for the customer.

Steven W. Kochensparger (Registered Principal, Upper Arlington, Ohio) was fined \$200,000, barred from association with any NASD member in any capacity, and required to pay restitution to a public customer.

The sanctions were based on findings that Kochensparger directly and indirectly, made false statements of material facts or omitted to state material facts, engaged in schemes to defraud and in acts, practices, or courses of business which defrauded lenders, insurers, and other institutions concerning purported bonds issued by the Government National Mortgage Association (GNMA). In each incident, Kochensparger made representations to a lender, seller, or insurance company that his member firm held certain GNMA bonds as collateral for particular transactions, such as loans or the sale of real estate when, in fact, the member firm never held any GNMA bonds for any customer. As a result of this activity, lenders lost millions of dollars.

In addition, Kochensparger received \$25,000 from a public customer to purchase shares in a fund that did not exist and, instead, purchased shares of Kochensparger's member firm without the customer's knowledge or consent. Kochensparger also effected two unauthorized transactions in a public customer's account.

Marc Peter Kopish (Registered Principal, Dallas, Texas) was fined \$20,000 and barred from associa-

tion with any NASD member in any capacity. The sanctions were based on findings that, without authority, Kopish co-signed a \$5,000 check drawn on the reserve account of a member firm with which he was neither registered nor associated. The check was sent to a public customer but was subsequently dishonored due to insufficient funds.

Ricardo Lavadores (Registered Representative, Chicago, Illinois) was fined \$21,500, barred from association with any NASD member in any capacity, and required to pay \$1,660.32 in restitution. The sanctions were based on findings that Lavadores obtained from insurance customers \$1,660.32 to pay insurance premiums but kept the funds for his personal use and benefit.

Adam Stuart Levine (Registered Representative, Port Washington, New York) was fined \$40,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following appeal of a decision by the DBCC for District 10. The sanctions were based on findings that Levine effected seven unauthorized transactions in public customer accounts. In addition, without the knowledge or consent of two public customers, Levine transferred their accounts from one member firm to another.

Levine appealed this action to the SEC, and the sanctions, other than the bar, are not in effect pending consideration of the appeal.

Gabriel Anthony Martinez (Registered Representative, Cypress Hills, New York) was fined \$40,000, barred from association with any NASD member in any capacity, and required to pay \$1,000 in restitution to his member

firm. The sanctions were based on findings that, without the knowledge or consent of 24 public customers, Martinez submitted dividend/loan/cash surrender request forms for their accounts, causing checks totaling \$24,748.33 to be issued. Martinez then forged the customers' signatures on the checks, deposited the funds into his bank account, and converted the proceeds to his own use and benefit. In addition, Martinez failed to respond to NASD requests for information.

Thomas Garth Nauman (Registered Representative, Elma, Washington) was fined \$20,000 and suspended from association with any NASD member in any capacity for 30 days. The sanctions were based on findings that Nauman wrongfully overtraded and failed to pay for multiple option transactions placed in his personal securities account.

Elizabeth Ann Paetow (Registered Principal, Waverly, Minnesota) submitted a Letter of Acceptance, Waiver and Consent pursuant to which she was fined \$20,000, barred from association with any NASD member in any capacity, and required to pay \$4,500 in restitution to entitled parties. Without admitting or denying the allegations, Paetow consented to the described sanctions and to the entry of findings that without her firm's knowledge or consent, she converted \$4,500 from the firm's cash account to her own use and benefit.

Joel E. Porter (Registered Representative, Birmingham, Alabama) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was barred from association with any NASD member in any capacity. Without admitting or denying the allega-

tions, Porter consented to the described sanction and to the entry of findings, among other things, that without the knowledge or consent of two public customers, he caused \$10,418.68 to be withdrawn from their accounts by endorsing checks in their names, thereby converting the funds to his own use and benefit.

Bart G. Pouwels (Registered Representative, Marrero, Louisiana) was fined \$30,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Pouwels received from an insurance customer a \$399 check to pay automobile insurance. According to the findings, Pouwels failed to buy the insurance and, instead, cashed the check and converted the funds to his own use and benefit without the customer's knowledge or consent. In addition, Pouwels failed to respond to NASD requests for information.

David Joseph Radzynski (Registered Representative, Thousand Oaks, California) was fined \$35,872 and barred from association with any NASD member in any capacity. However, he can reduce the fine if he proves to the District 2 office that he has made restitution to the applicable party.

The sanctions were based on findings that Radzynski asked a public customer to pay for commissions generated after executing an order to purchase securities in the customer's account. Radzynski received an \$872 check from the customer and explained he would reimburse the customer when he received the commission payment from his member firm. Radzynski cashed the check but did not repay the customer. Moreover, Radzynski solicited

the aforementioned purchase prior to requalifying in any capacity to associate with a broker/dealer.

Radzyski also failed to respond to NASD requests for information.

Rodney Rigsby (Registered Principal, Nashville, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Rigsby consented to the described sanction and to the entry of findings that he allowed his member firm to engage in a securities business while its net capital was below the required minimum, and failed to prepare an accurate computation of the firm's net capital.

The NASD also found that Rigsby withdrew \$3,000 from his member firm's clearing account and directed that the funds be wired to his personal bank account, thereby converting the funds to his own use and benefit without the firm's knowledge or consent. In addition, the findings stated that Rigsby paid a representative of another member firm \$328.43 in connection with three transactions involving corporate securities.

Vernon Robinson (Associated Person, Culver City, California) was fined \$40,207.50 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Robinson accepted from an insurance customer \$249 to purchase an insurance policy. Robinson submitted only \$41.50 of the funds towards the purchase and converted the remaining \$207.50. Also, Robinson failed to respond to NASD requests for information.

James Russen, Jr. (Registered

Representative, Middle Island, New York) was fined \$50,000 and suspended from association with any NASD member in any capacity for 30 business days. The NBCC imposed the sanctions following an appeal of a decision by the DBCC for District 10. The sanctions were based on findings that Russen executed unauthorized transactions in the accounts of four public customers at four different member firms.

Russen has appealed this action to the SEC, and the sanctions are not in effect pending consideration of the appeal.

Michael Clayton Saunders (Registered Representative, Kansas City, Missouri) was fined \$5,000 and suspended from association with any NASD member in any capacity. The suspension commenced November 9, 1992, and will continue until Saunders demonstrates to the NASD's District 4 staff that he has either fully paid the arbitration award or has been released from paying it. The sanctions were based on findings that Saunders failed to pay a \$36,196.18 arbitration award.

Richard C. Stoyeck (Registered Representative, New York, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000, required to pay \$17,025 in restitution to public customers, and suspended from association with any NASD member in any capacity for five business days. Without admitting or denying the allegations, Stoyeck consented to the described sanctions and to the entry of findings that he executed trades for public customers and charged them excessive gross sales credits ranging from 18 to 20 percent of the total cost of the trade.

Bruce Edward Straughn (Registered Representative, Naperville, Illinois) was suspended from association with any NASD member in any capacity for five business days. The sanction was based on findings that Straughn failed to pay a \$15,000 NASD arbitration award.

Dana H. Taylor (Registered Representative, Washington Courthouse, Ohio) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$4,700, barred from association with any NASD member in any capacity, and required to pay \$779.10 in restitution to his member firm. Without admitting or denying the allegations, Taylor consented to the described sanctions and to the entry of findings that he misappropriated and converted to his own use insurance-customer funds totaling \$779.10. According to the findings, these funds represented loan proceeds from insurance policies that were obtained without a customer's knowledge or consent and the cash surrender value of two other insurance policies that the same customer wanted used to pay for an additional insurance policy.

David M. Vincent (Registered Representative, Louisville, Kentucky) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000, suspended from association with any NASD member in any capacity for one week, and suspended from association with any NASD member in any options-related activity for one year. Without admitting or denying the allegations, Vincent consented to the described sanctions and to the entry of findings that he exercised discretion in the accounts of public customers without either their prior written authorization or his member

firm's prior written acceptance of the accounts as discretionary.

The NASD also found that, in executing five transactions, Vincent traded beyond the approved option level in the public customer's account. In addition, the NASD determined that Vincent engaged in an options transaction in a public customer's account without having reasonable grounds for believing that the transaction was suitable for the customer.

Troy Wetter (Registered Principal, Greenview, Illinois) was fined \$50,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following appeal of a decision by the DBCC for District 8. The sanctions were based on findings that a former member firm, acting through Wetter, failed to maintain its minimum required net capital and prepared inaccurate net capital computations. Furthermore, the firm, acting through Wetter, filed inaccurate FOCUS Parts I and II reports and failed to file its audit report in a timely manner. In addition, the firm, acting through Wetter, conducted a securities business when the firm was suspended from membership in the NASD.

This action has been appealed to the SEC and the sanctions, other than the bar, are not in effect pending consideration of the appeal.

Wayne Wheeler (Registered Principal, Florida, New York) was fined \$75,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that, in various securities transactions, Wheeler engaged in fraudulent and manipulative practices including misrepresentations, unauthorized transactions, conversion of cus-

tomers funds, private securities transactions, and forgery. In addition, Wheeler failed to respond to NASD requests for information.

Francis Eldon Willock (Registered Representative, Santa Ana, California) was barred from association with any NASD member in any capacity. The sanctions were based on findings that Willock made material misrepresentations to foreign lending institutions to induce the purchase of annuity contracts by an insurance customer.

Frank L. Wolff (Registered Representative, Farmington Hills, Michigan) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$50,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Wolff consented to the described sanctions, and to the entry of findings that he signed an insurance customer's name to an "Authorization to Terminate Insurance Form" without the customer's knowledge or consent resulting in the issuance of a \$3,616 check. According to the findings, Wolff issued a stop payment on the check and requested that a replacement check be sent to his home address. The NASD determined that Wolff used the proceeds of the replacement check for purposes other than for the benefit of the customer.

The NASD also found that Wolff obtained four checks totaling \$5,332.66 made payable to public customers by either requesting that the checks be sent to his home address or to his business address without the customers' knowledge or consent. The findings stated that Wolff failed to forward the checks to the customers and used the funds for other purposes.

Wolff also failed to respond to NASD requests for information.

Dario A. Zgoznic (Registered Representative, Eastlake, Ohio) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$70,000, barred from association with any NASD member in any capacity, and required to pay \$32,521.02 in restitution to his member firm. Without admitting or denying the allegations, Zgoznic consented to the described sanctions and to the entry of findings that he misappropriated and converted to his own use customer funds totaling \$32,521.02. These funds represented the proceeds of the liquidation of a mutual fund and unauthorized distributions from the life insurance policies of customers.

Mark C. Zielberg (Associated Person, Louisville, Kentucky) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Zielberg consented to the described sanctions and to the entry of findings that he wrongfully caused five deposits totaling \$1,160 to be shown in his personal checking account at his member firm by falsely recording a transfer of funds from the cash portion of his account. The NASD found that Zielberg failed to submit the checks corresponding to the funds withdrawn until a later date.

Individuals Fined

Jay M. Fertman (Registered Principal, Castle Rock, Colorado) was fined \$76,964.62 and required to requalify before acting in any capacity with an NASD member firm. The sanctions were based on

findings that Fertman failed to disclose to customers that they were charged unfair and unreasonable prices on principal sales of stock by his member firm. Furthermore, Fertman either solicited the customers to purchase the aforementioned stock, or otherwise caused customer orders to be received and processed for purchases of these securities at unfair and unreasonable prices.

Firms Expelled for Failure to Pay Fines and Costs in Connection With Violations

Dania Securities, Incorporated, Newport Beach, California

DeLaureal, Munroe Securities Corporation, New York, New York

First Choice Securities Corporation, Englewood, Colorado

LaBrec Securities, Incorporated, Nashville, Tennessee

Osborne, Stern & Company, Incorporated, Los Angeles, California

Pacific Integrated Group, Incorporated, Santa Clara, California

Walbridge Securities, Incorporated, N/K/A Aztec Securities, Incorporated, Fort Worth, Texas

Firms Suspended

The following firms were suspended from membership in the NASD for failure to comply with formal written requests to submit financial information to the NASD. The actions were based on the provisions of Article IV, Section 5 of the NASD Rules of Fair Practice and Article VII, Section 2 of the NASD By-Laws. The date the suspension commenced is listed after each entry. If the firm has complied with the request for information, the listing also includes the date the suspension concluded.

Brighton Financial Corporation, Inc., Houston, Texas (December 4, 1992)

CG Financial Services, Inc., Burbank, California (December 4, 1992)

Smetek, Van Horn and Cormack, Inc., Houston, Texas (December 4, 1992)

Individuals Whose Registrations Were Revoked for Failure to Pay Fines and Costs in Connection With Violations

William M. Boland, Jr., New York, New York

Garrison D. Bye, Tampa, Florida

William J. Caltabiano, Jr., Massapequa Park, New York

Linda C. Chandler, Fernandina Beach, Florida

James C. Hale, Richardson, Texas

Leonce Hampton, Jr., New Orleans, Louisiana

Lawrence M. Henley, Scottsdale, Arizona

Edmund F. Konczakowski, Pompano Beach, Florida

Mark Lopergola, Philadelphia, Pennsylvania

Ridge B. McMichael, Ft. Worth, Texas

Douglas W. Osborne, Sr., Venice, California

Charles E. Perna, Jensen Beach, Florida

Norman E. Phillips, Brooklyn, New York

Arthur M. Schneider, Old Bethpage, New York

Dale D. Schwartzenhauer, Sandy, Oregon

Michael D. Stewart, Cambridge, England

Gregory F. Walsh, Los Angeles, California

FOR YOUR INFORMATION

Bulletin Board Designated As “Qualifying Electronic Quotation System”

On December 30, 1992, the Securities and Exchange Commission (SEC) granted the NASD’s request for interim designation of the OTC Bulletin Board® service (OTCBB) as a “Qualifying Electronic Quotation System” for purposes of certain penny-stock rules that became effective on January 1, 1993. The SEC adopted these rules pursuant to the Securities Enforcement Remedies and Penny Stock Reform Act of 1990. Essentially, this action permits broker/dealers to utilize inside bid/ask prices displayed in the OTCBB to make certain price determinations and disclosures that are now required by the new rules.

Generally, these rules apply to broker/dealer transactions in penny stocks with or for customer accounts. The SEC’s designation of the OTCBB as a qualifying system should facilitate a broker/dealer’s compliance with Securities Exchange Act Rules 15g-3, 15g-4, and 15g-6. Additionally, the designation will assist firms in determining whether a security’s price (based on an inside bid) causes it to be classified as a penny stock under Securities Exchange Act Rule 3a51-1. If you have any questions, please contact Michael Kulczak in the General Counsel’s Office at (202) 728-8811 or Susan McDougall in Trading & Market Services at (202) 728-8150.

SEC Participates in CRD Phase II

Effective January 25, 1993, the Central Registration Depository (CRD) will begin processing broker/dealer filings for the Securities and Exchange Commission (SEC). Member firms that amend their

Uniform Application for Broker-Dealer Registration (Form BD) on or after that date need only file the change with the NASD.® Because it will be able to review those amendments through CRD, the SEC will no longer accept hard-copy filings. For further details please refer to SEC Release No. 34-31660.

The SEC and the NASD view this as a major step toward “one stop” filing for the broker/dealer community because it eliminates the burden of duplicative filings.

Currently, 49 states and the Chicago Board of Options Exchange participate in CRD Phase II. Member firms considering registration changes should contact specific jurisdictions to determine if any submissions in addition to those made to CRD are necessary.

In the same release, the SEC authorized the NASD to process Form BD applications and *Uniform Request for Broker-Dealer Withdrawal* (Form BDW) on its behalf. The SEC will use CRD to review initial applications filed with the NASD and will accept them if all SEC criteria are met.

In addition, filing the Form BDW with the CRD for processing will constitute filing with the SEC. If you have any questions regarding these changes, call NASD Member Services Phone Center at (301) 590-6500.

North Carolina Increases Agent Registration, Re-registration, and Renewal Fees

Effective January 1, 1993, North Carolina increased its agent fees. Agent registration, re-registration, and renewal fees rose from \$45 to \$55. Agent renewal fees also increased to \$55. This increase was

effective with the 1992-93 renewal program. If you have any questions regarding these changes, call NASD Member Services Phone Center at (301) 590-6500.

Operation of The Nasdaq Stock MarketSM on December 31, 1993

The Nasdaq Stock MarketSM and the securities exchanges will be open for trading on December 31, 1993. When a determination is made concerning the observance of New Year's Day, January 1, 1994, information will be circulated regarding the trade date-settlement date schedule.

Questions regarding this item should be directed to the Uniform Practice Department at (212) 858-4341.

NASD Member Voting Results

As a member service, the NASD publishes the result of member votes on issues presented to them for approval in the monthly *Notices to Members*. Most recently, members voted on the following issues:

- **Notice to Members 92-56** —

Proposed Recision of the Guidelines Regarding Communications With the Public About Investment Companies and Variable Contracts (Guidelines) and Proposed Amendments to Article III, Section 35 of the Rules of Fair Practice to Incorporate Items From the Guidelines. Ballots For: 1,768; Against: 154; and Unsigned: 18.

- **Notice to Members 92-57** — Proposed Amendments to Schedule E to the NASD By-Laws Regarding Potential Conflicts of Interest. Ballots For: 1,675; Against: 231; and Unsigned: 29.

Questions regarding this item should be directed to Stephen Hickman, President's Office, at (202) 728-8381.

NASD Mails New Edition of *Guide to Information & Services*

With this issue of *Notices to Members*, NASD members are receiving the December 1992 edition of the *NASD Guide to Information & Services*. This publication, updated semiannually, is arranged by subject and includes names and phone numbers of persons members may call for infor-

mation and assistance.

Questions regarding this item may be directed to Sharon Lippincott, Communication Services, at (202) 728-8278.

What Do You Think of Our New Look?

Beginning with this edition, *Notices to Members* incorporates a modern look to make it more appealing and easier to read. This redesign is part of a general reformatting of all NASD publications that will continue through the coming year.

These changes are also intended to facilitate production of next year's edition of the *Notices to Members* bound volume collection. These *Notices to Members* bound volumes provide you with each year of *Notices* in a handy, ready-to-use format.

For more information on NASD publications, please call NASD Corporate Communications at (202) 728-6900. Or, if you have any questions or comments on *Notices*, please direct them to Thomas Mathers, Editor, at (202) 728-8267 or Sharon Lippincott, Associate Editor, at (202) 728-8278.

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NASD NOTICE TO MEMBERS 93-8

SEC Approval of Amendment Relating To the Payment of Gratuities or Anything Of Value by Members To Others

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On December 28, 1992, the Securities and Exchange Commission (SEC) approved and made effective an amendment to Article III, Section 10(a) of the Rules of Fair Practice. The amendment raises from \$50 to \$100 the maximum value of gifts or gratuities a member or associated person may provide to another person each year. The text of the amendment follows this Notice.

Background and Description of The Amendment

The SEC has approved an amendment to Article III, Section 10(a) of the Rules of Fair Practice that raises from \$50 to \$100 the maximum per person value of gratuities or gifts a member or associated person may provide to another person each year.

Article III, Section 10(a) of the NASD Rules of Fair Practice sets an annual, per person limit on payments of anything of value, including gifts and gratuities, by a member or associated person of a member to another person where the payment relates to the business of the recipient's employer. The rule protects against improprieties that might arise when members or associated persons give substantial gifts or monetary payments to certain persons without their employer's knowledge. The amendment only raises the dollar limit in the rule; it does not change the categories of persons covered by the rule or the other requirements under Section 10 concerning prior written agreements and recordkeeping relating to such compensation for services.

The proposed rule change is consistent with recently approved Rule 350(a) of the New York Stock Exchange (NYSE), which raised to \$100 from \$50 the amount of a gratuity which a NYSE member may give to another without obtaining prior written consent of the recipient's employer. The NASD's new rule simplifies compliance by member firms that also belong to the NYSE.

Questions concerning this Notice should be directed to Elliott R. Curzon, Senior Attorney, Office of General Counsel, at (202) 728-8407.

Amendment to Article III, Section 10 Of the Rules of Fair Practice

(Note: New text is underlined; deleted text is in brackets.)

Influencing or Rewarding Employees of Other

Sec. 10

(a) No member or person associated with a member shall, directly or indirectly, give or permit to be given anything of value, including gratuities, in excess of one hundred [fifty] dollars per individual per year to any person, principal, proprietor, employee, agent or representative of another person where such payment or gratuity is in relation to the business of the employer of the recipient of the payment or gratuity. A gift of any kind is considered a gratuity.

NASD NOTICE TO MEMBERS 93-9

SEC Approves Amendments to NASD® Rules Governing Transaction Reporting

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On December 14, 1992, the Securities and Exchange Commission (SEC) approved a series of changes to the NASD® rules governing transaction reporting in Nasdaq National Market,® Nasdaq Small-Cap,SM and exchange-listed securities. These changes eliminate certain inconsistencies among parallel rules covering Nasdaq® securities and recognize the Automated Confirmation Transaction (ACTSM) service as the principal vehicle for reporting transactional data between the hours of 9:30 a.m. and 5:15 p.m., Eastern Time (ET), on each business day. Additionally, the amended rules eliminate the minimum activity thresholds for real-time reporting by firms that are not registered market makers in the affected securities. All of the modified rules will take effect on March 8, 1993.

Background and Description of Amendments

On December 14, 1992, the SEC approved various amendments to the NASD rules that prescribe trade-reporting requirements for members' transactions in Nasdaq National Market, Nasdaq Small-Cap, and exchange-listed securities. Overall, these amendments make the terminology and reporting procedures more consistent, recognize ACT as the primary vehicle for reporting over-the-counter transactions in equity securities, and reduce manual reporting of transactional data on Form T. Although largely technical in nature, the changes facilitate member compliance with the reporting rules and optimize the automated capture of trade details for both operational and regulatory purposes.

Part XII of Schedule D of the NASD By-Laws applies exclusively to the reporting of transactional data on Nasdaq National Market securities. It has been modified in the following respects. First, changes to the opening paragraph and Sections 1 and 2 delete outmoded references to reporting mechanisms that have been replaced by ACT and the support facilities of the ACT service desk in New York City. Second, Section 2(a)(2) has been amended to eliminate the *de minimis* thresholds for real-time reporting of transactions by a member firm that is not a registered market maker in a given Nasdaq National Market security. For example, if a firm acts as a dual agent and crosses two customer orders in a stock in which it is not a registered market maker, the firm will now be required to report that trade through ACT within 90 seconds of execution, regardless of the magnitude of the firm's recent trading activity in that stock or other Nasdaq National Market issues. Ordinarily, this trade will be reported through an authorized Nasdaq Workstation® PC or the firm's Computer-to-Computer Interface (CTCI) with the ACT processor. The reporting of trades by telephone to the ACT service desk will continue to be limited to firms without access to Nasdaq equipment and that have averaged five or fewer trades per day during the preceding calendar quarter. Of course, firms unable to report directly into ACT due to a system or transmission failure may still satisfy their trade-reporting obligations by telephoning the NASD's Market Operations Department in New York City.

The amendments to Sections 2(a)(3), (4), and (5) of Part XII will permit manual trade reporting via Form T in fewer instances because of the elimination of the thresholds

for real-time reporting by firms classified as non-market makers or “non-registered reporting members.” Additionally, Section 2(a)(5) now limits Form T reporting to trades executed outside the hours that ACT is available to accommodate trade reports from the U.S. market session, 9:30 a.m. to 5:15 p.m., ET. Finally, Section 2(a)(4) incorporates new language specifying that trades executed between the hours of 4 and 5:15 p.m., ET, are reportable within 90 seconds after execution and that such trades must be designated as “.T” or after-hours trades. This change reflects an expansion of the .T reporting procedure to all trades in Nasdaq National Market issues that are executed after 4 p.m., ET, and reported into ACT. (Currently, the .T reporting procedure does not begin until 4:10 p.m., ET.) The foregoing change is intended to differentiate more clearly, via the trade-reporting process, all trades executed in Nasdaq National Market securities after the 4 p.m., ET, close of the Nasdaq market and before ACT closes at 5:15 p.m., ET. Nonetheless, trades executed during normal business hours but reported as late trades after 4 p.m., ET, will be accepted with a late indicator (.SLD) until 4:39 p.m., ET.

Part XIII of Schedule D contains the trade-reporting requirements applicable to members’ trades in Nasdaq Small-Cap securities. Part XIII has been modified to reflect the following: (1) elimination of the activity thresholds for real-time reporting by any member firm that is not a registered market maker in a given Nasdaq Small-Cap security; (2) limitation of transactional reporting via Form T to members’ transactions executed outside the hours of 9:30 a.m. to 5:15 p.m., ET, on each U.S. business day; (3) expansion of the .T reporting pro-

cess to all trades executed after the 4 p.m., ET, close of the Nasdaq market and before ACT closes at 5:15 p.m., ET; and (4) clarification that the 90-second trade-reporting requirement encompasses after-hours trades executed between 4 p.m. and 5:15 p.m., ET, and reported into ACT. Essentially, these amendments are designed to ensure uniformity in the reporting procedures applicable to members’ transactions in either Nasdaq Small-Cap or Nasdaq National Market securities.

The recent amendments to Schedule G to the NASD By-Laws (which governs trade reporting in exchange-listed securities) track most of the changes being made to Parts XII and XIII of Schedule D. The major exception involves definitional changes in Section 1 of Schedule G. First, the terms “Registered Reporting Member” and “Non-Registered Reporting Member” are being substituted for “Designated Reporting Member” and “Non-Designated Reporting Member” in Sections 1(c) and 1(e), respectively. These definitions distinguish, for trade-reporting purposes, between NASD members that are either registered as Consolidated Quotation System (CQS) market makers in a given security and members that are not so registered. Second, clarifying language has been added to Section 1(c) to indicate that a member has the status of a “Registered Reporting Member” solely in those listed securities in which it has registered with the NASD as a CQS market maker. Without such registration in a given CQS security, the firm is deemed to be a “Non-Registered Reporting Member” for purposes of its trade-reporting obligations in that issue under Schedule G. This change serves to conform Schedule G to Parts XII and XIII of Schedule

D in terms of defining market makers and non-market makers on a security-by-security basis.

Lastly, it should be noted that the foregoing amendments do not alter the established conventions in Parts XII and XIII of Schedule D and in Schedule G for determining which party has the obligation of entering a transaction report. The amended rules will take effect on March 8, 1993.

Questions regarding this Notice can be directed to Michael J. Kulczak, Associate General Counsel, NASD Office of General Counsel at (202) 728-8811. Specific questions on the application of the NASD’s trade-reporting rules can be directed to NASD Market Surveillance staff members Barbara Neurell or Mary Rose Murray at (800) 925-8156 or (301) 590-6080.

Amendments to Parts XII and XIII Of Schedule D and Schedule G to The NASD By-Laws

(Note: New text is underlined; deleted text is in brackets.)

Part XII

Reporting Transactions in Nasdaq National Market Designated Securities

This part has been adopted pursuant to Article VII of the Corporation’s By-Laws and applies to the reporting by all members of transactions in NASDAQ/National Market System securities (“designated securities”) through the [Transaction Reporting System] Automated Confirmation Transaction Service (“ACT”).

* * * * *

Section 1 — Definitions

* * * * *

(b) [“Transaction Reporting System” means the transaction reporting system for the reporting and dissemination of last sale reports in designated securities.] “Automated Confirmation Transaction Service” or “ACT” is the service that, among other things, accommodates reporting and dissemination of last sale reports in designated securities.

* * * * *

Section 2 — Transaction Reporting

(a) When and How Transactions are Reported

(1) Registered Reporting Market Makers shall, [transmit through the Transaction Reporting System,] within 90 seconds after execution, transmit through ACT last sale reports of transactions in designated securities executed during [the] normal market hours, [of the] Transaction Reporting System. Transactions not reported within 90 seconds after execution shall be designated as late.

(2) Non-Registered Reporting Members shall, within 90 seconds after execution, transmit through ACT or the ACT Service Desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to the Market Operations Department in New York City, last sale reports of transactions in designated securities executed during normal market hours. [transmit through the Transaction Reporting System, or if such System is unavailable, via Telex, TWX or telephone to the NASDAQ Operations Department in New

York City, within 90 seconds after execution, last sale reports of transactions in designated securities executed during the trading hours of the Transaction Reporting System unless all of the following criteria are met:

(A) The aggregate number of shares of designated securities which the member executed and is required to report during the trading day does not exceed 1,000 shares; and

(B) The total dollar amount of shares of designated securities which the member executed and is required to report during the trading day does not exceed \$25,000; and

(C) The member’s transactions in designated securities have not exceeded the limits of (A) or (B) above on five or more of the previous ten trading days.]

Transactions not reported within 90 seconds after execution shall be designated as late. [If the member has reason to believe its transactions in a given day will exceed the above limits, it shall report all transactions in designated securities within 90 seconds after execution; in addition, if the member exceeds the above limits at any time during the trading day, it shall immediately report and designate as late any unreported transactions in designated securities executed earlier that day.]

(3) Non-Registered Reporting Members shall report weekly to the Market [NASDAQ] Operations Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities which are not required to be reported under paragraph (2) or (4). [by paragraph (2) to be reported within 90 seconds after execution.]

(4) Last sale reports of transactions in designated securities executed between the hours of 4:00 p.m. and [5:00] 5:15 p.m. Eastern Time shall be transmitted through [the Transaction Reporting System no later than 5:00 p.m. Eastern Time] ACT within 90 seconds after execution; trades executed and reported after 4:00 p.m. Eastern Time shall be designated as “.T” or after hours trades.

(5) All members shall report weekly to the [NASDAQ] Market Operations Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities executed outside the hours of 9:30 a.m. and 5:15 [5:00] p.m. Eastern Time.

* * * * *

Part XIII

Reporting Transactions in Nasdaq Small-CapSM Securities

This Part has been adopted pursuant to Article VII of the Corporation’s By-Laws and sets forth the applicable reporting requirements for transactions in Nasdaq Small-CapSM securities (“designated securities”), [that are not classified as Nasdaq/National Market System securities.] Members shall utilize the Automated Confirmation Transaction Service (“ACT”) for transaction reporting.

* * * * *

Section 2 — Transaction Reporting

(a) When and How Transactions are Reported

* * * * *

(2) Non-Registered Reporting Members shall, within 90 seconds

after execution, transmit through ACT or the ACT service desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to the Market Operations Department in New York City, last sale reports of transactions in designated securities executed during normal market hours, [unless all of the following criteria are met:

(A) The aggregate number of shares of designated securities which the member executed and is required to report during the trading day does not exceed 1,000 shares; and

(B) The total dollar amount of shares of designated securities which the member executed and is required to report during the trading day does not exceed \$25,000; and

(C) The member's transactions in designated securities have not exceeded the limits of (A) or (B) above on five or more of the previous ten trading days.]

Transactions not reported within 90 seconds after execution shall be designated as late. [If the member has reason to believe its transactions in a given day will exceed the above limits, it shall report all transactions in designated securities within 90 seconds after execution; in addition, if the member exceeds the above limits at any time during the trading day, it shall immediately report and designate as late any unreported transactions in designated securities executed earlier that day.]

(3) Non-Registered Reporting Members shall report weekly to the [Nasdaq] Market Operations Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities

which are not required to be reported under paragraph (2) or (4). [by paragraph (2) to be reported within 90 seconds after execution.]

(4) Last sale reports of transactions in designated securities executed between the hours of 4:00 p.m. and 5:15 [5:00] p.m. Eastern Time shall be transmitted through [the] ACT [system] within 90 seconds after execution; trades executed and reported after [4:10] 4:00 p.m. Eastern Time shall be designated as ".T" or after hours trades.

(5) All members shall report weekly to the [Nasdaq] Market Operations Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities executed outside the hours of 9:30 a.m. and 5:15 [5:00] p.m. Eastern Time.

* * * * *

Schedule G

Reporting Transactions in Listed Securities

* * * * *

Section 1 — Definitions

* * * * *

(c) "Registered [Designated] Reporting Member" means a member of the Association that is registered as a CQS Market Maker [in an eligible security], pursuant to Part VII of Schedule D of the Association's By-Laws, in a particular eligible security. A member is a Registered Reporting Member in only those eligible securities for which it has registered as a CQS market maker. A member shall cease being a Registered Reporting Member in an eligible security when it has withdrawn or voluntari-

ly terminated its quotations in that security or when its quotations have been suspended or terminated by action of the Corporation.

* * * * *

(e) "Non-Registered [Designated] Reporting Member" means [all] a member[s] of the Association that [which are] is not a Registered [Designated] Reporting Member[s].

(f) "Automated Confirmation Transaction Service" or "ACT" is the service that, among other things, accommodates reporting and dissemination of last sale reports in eligible securities.

Section 2 — Transaction Reporting

(a) When and How Transactions are Reported

(1) Registered [Designated] Reporting Members shall transmit through ACT, [the NASDAQ Transaction Reporting system,] within 90 seconds after execution, last sale reports of transactions in eligible securities executed during the trading hours of the Consolidated Tape otherwise than on a national securities exchange. Registered [Designated] Reporting Members shall also transmit through ACT, [the NASDAQ Transaction Reporting System,] within 90 seconds after execution, last sale reports of transactions in eligible securities executed in the United States otherwise than on a national securities exchange between 4:00 p.m. and 5:15 p.m. Eastern Time. Transactions not reported within 90 seconds after execution shall be designated as late.

(2) Non-Registered [Designated] Reporting Members shall, within 90 seconds after execution, transmit through ACT or the ACT Service

Desk (if qualified pursuant to Part IX of Schedule D to the NASD By-Laws), or if ACT is unavailable due to system or transmission failure by telephone to the Market Operations Department in New York City, [the Transactions Reporting System, or if such System is unavailable, via Telex, TWX or telephone, to the NASDAQ Department in New York City, within 90 seconds after execution,] last sale reports of transactions in eligible securities executed during the trading hours of the Consolidated Tape otherwise than on a national securities exchange. [unless all of the following criteria are met:

(A) The aggregate number of shares of eligible securities which the member executed and is required to report does not exceed 1,000 shares in any one trading day; and

(B) The total dollar amount of shares of eligible securities which the member executed and is required to report does not exceed \$25,000 in any one trading day; and

(C) The member's transactions in eligible securities have not exceeded the limits of (A) or (B) above on five or more of the previous ten trading days.]

Non-Registered [Designated] Reporting Members shall [transmit through the NASDAQ Reporting System, or if such System is unavailable, via Telex, TWX or telephone, to the NASDAQ Department in New York City], within 90 seconds after execution, transmit through ACT or the ACT service desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to the Market Operations Department in New York City, last sale reports of transactions in eligible securities executed in the United States otherwise than on a national securities exchange between the hours of 4:00 p.m. and 5:15 p.m. Eastern Time, [unless all of the criteria specified in paragraphs (A), (B) and (C) above are met.]

Transactions not reported within 90 seconds after execution shall be designated as late. [If the member has reason to believe its transactions in a given day will exceed the above limits, it shall report all transactions in eligible securities within 90 seconds after execution; in addition, if the member exceeds the above limits at any time during the trading day, it shall immediately report and designate as late any unreported transactions in eligible securities executed earlier that day.]

(3) Non-Registered [Designated] Reporting Members shall report weekly to the [NASDAQ] Market Operations Department in New York City, on Form T, last sale reports of transactions in eligible securities that [which] are not required [by paragraph (2)] to be reported [within 90 seconds after execution] under paragraph (2).

* * * * *

(b) Which Party Reports Transaction

* * * * *

(2) In transactions between two Registered [Designated] Reporting Members, only the member representing the sell side shall report.

(3) In transactions between a Registered [Designated] Reporting Member and a Non-Registered [Designated] Reporting Member, only the Registered [Designated] Reporting Member shall report.

(4) In transactions between [the] Non-Registered [Designated] Reporting Members, only the member representing the sell side shall report.

* * * * *

NASD NOTICE TO MEMBERS 93-10

Request for Comments On Proposed Amendment to the Corporate Financing Rule Relating to the Fairness And Reasonableness of Underwriter Warrant's Anti-Dilution Provisions

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD® requests comment on a proposed amendment to the Corporate Financing Rule under Article III, Section 44 of the Rules of Fair Practice intended to regulate the anti-dilution provisions of warrants received as underwriting compensation. The amendment would provide that underwriters and related persons may not receive warrants as compensation if the warrant contract includes anti-dilution provisions with disproportionate rights, privileges, and economic benefits that are not provided to existing shareholders of a company or to investors purchasing the company's securities in a public offering. The text of the proposed amendment follows this Notice.

Background

The NASD's Corporate Financing Committee (Committee) has reviewed the anti-dilution provisions of warrants received as underwriting compensation by members participating in public offerings of securities. In some instances, the underwriter's warrants acquired by member firms have included arrangements that appear to be unfair and unreasonable under the Corporate Financing Rule, Article III, Section 44 of the Rules of Fair Practice (Rule). Documents filed with the Securities and Exchange Commission (SEC) in 1991 regarding the Rule included a suggestion to clarify the provisions of Subsection (c)(6)(B)(vi)(7) by excluding from its scope any inference that the anti-dilution provisions of an underwriter's warrant could be viewed as unfair or unreasonable because its terms would permit an underwriter to exercise or convert the warrant on terms more favorable than the terms of the securities being offered to the pub-

lic. The NASD rejected that position because it had recently reviewed a number of anti-dilution provisions that appeared to give underwriters the ability to acquire stock substantially in excess of the Rules' Stock Numerical Limitation, and exercise the warrant at prices substantially below the price established at the date of grant. The Committee also concluded that warrants received by members as compensation for a public offering should not be structured to provide these types of disproportionate benefits through the operation of anti-dilution provisions.

The Committee believes that the underlying principle guiding the application of the Rule to anti-dilution provisions of warrants acquired as compensation in public offerings should be to ensure that an underwriter does not negotiate to receive securities as underwriting compensation that contain terms more favorable than the terms of the securities offered to the public. Since an underwriter should not receive securities on terms more favorable than its customers, the anti-dilution clauses pertaining to any warrants received as compensation should not provide a potential for economic benefit that is not also received by the purchasers of the securities offered to the public.

Overall, the Committee believes that the anti-dilution rights associated with any security acquired as compensation by a member in a public offering should not put the member at an advantage over its customers based on the occurrence of any event affecting the issuer's capitalization. Accordingly, anti-dilution clauses should provide an underwriter only with those benefits it would have received had the warrant been exercised immediately before any event.

The Committee also believes that the provisions of an underwriter's warrant should encourage a commonality of interest by the underwriter, issuer, and public investors. Thus, the member should have an incentive to follow the company's progress and provide research and trading support to the stock in the aftermarket. Any clauses of a warrant contract that provide a member with an incentive that may be inconsistent with these premises are inappropriate.

The proposal would prohibit anti-dilution provisions of underwriter's warrants that provide all the benefits of a shareholder plus various degrees of protection not afforded to public shareholders. These include provisions that provide protection from dilution or adjustments to exercise price in the event of new issuances of securities in public or private offerings, stock option plans, or the conversion of existing convertible securities. These types of anti-dilution protections are common in agreements designed to protect venture capital investors that have taken on the bona fide investment risk of providing early stage financing. However, the Committee does not believe such protections are appropriate in underwriter's warrant contracts where the underlying service provided is a distribution of securities and the warrants are part of a compensation package.

Findings by the Committee

The Committee reviewed a number of underwriter's warrant agreements to determine the nature of the various anti-dilution clauses contained in these documents. In general, anti-dilution clauses can be divided into two distinct classes:

- **Proportionate Benefits:** These provide customary anti-dilution adjustments to exercise price and number of securities in response to events affecting all shareholders such as, among others, stock dividends, combinations, reclassifications, and recapitalizations that entitle the underwriter to participate in the event as if it had been a shareholder before the event. These standard anti-dilution rights do not protect from dilution caused by new public or private issuances of securities or issuances under stock option plans. In addition, the rights generally assume the warrant has been exercised to determine any required adjustments.

- **Disproportionate Benefits:** These provide the holder of the warrant with all shareholder benefits, as well as varying degrees of protection from dilution by any new issuances of securities. This category may provide adjustments in the event of issuances under stock option plans, the conversion of existing convertible securities, and may even provide for the receipt of accrued cash dividends where dividends are declared before exercise of the warrant. Adjustments to exercise price and number of shares in response to new issuances of securities include variations which "weight" the effect of changes in the company's capitalization and also those which "ratchet" the adjustment without regard to the actual dilutive affect of the new issuance of securities.

Certain warrant contracts in this category can include anti-dilution clauses that provide adjustments to exercise price and number of shares that far exceed the actual dilution experienced by the holder of the warrant. Such clauses can penalize an issuer by causing the exercise price for the entire warrant to drop in response to the issuance of a

single option to an employee. This "ratchet" type adjustment mechanism, if triggered repeatedly, can result in the exercise price of an underwriter's warrant dropping to a price far below the price of the new issuance that triggered the anti-dilution clause. This is because the underwriter's exercise price is typically reduced with each issuance below either the market price of the issuer's shares or the exercise price of the warrant, resulting in the underwriter's exercise price being ratcheted lower with each successive issuance but never readjusting upwards.

In addition to wholesale reductions in the exercise price without giving effect to the price or number of shares sold, certain warrant contracts can further penalize the issuer by increasing the amount of shares subject to the warrant without any relationship to actual dilution (i.e., if one option is issued at half the underwriter's warrant exercise price, the underwriter's warrant will become exercisable at half the original price for double the original amount of shares). The Committee believes that such anti-dilution clauses should also be considered unfair and unreasonable under the Rule.

Explanation of Amendment

As noted above, adjustments to exercise price and number of shares that result from these unfair provisions include variations which "weight" the effect of changes in the company's capitalization and those that "ratchet" the adjustment without regard to the actual effect of the new issuance of securities. These provisions are constructed in a manner that provides disproportionate benefits to an underwriter relative to public shareholders or provides benefits that are simply

unique to the underwriter, such as the accrual of cash dividends relating to the securities underlying the underwriter's warrant.

The proposed rule language reflects the general fairness standard held by the Committee that it is inequitable for the underwriter to receive rights, privileges, or economic benefits that are more favorable than the benefits received by public investors who purchase securities in public offerings. Specifically, the rule language prohibits the grant of any anti-dilution privilege to the underwriter and related person that is not also available to shareholders or investors.

Request for Comments

The NASD asks members and other interested persons to comment on

the proposed amendment to the Corporate Financing Rule. Comments should be directed to:

Mr. Stephen D. Hickman
Corporate Secretary
National Association of Securities Dealers, Inc.
1735 K Street, NW
Washington, DC 20006-1500.

Comments must be received **no later than March 31, 1993**. Comments received by this date will be considered by the Corporate Financing Committee and the Board of Governors. Before becoming effective, the proposed amendment must be approved by the Board, adopted by the membership, and filed with the SEC for final approval.

Questions concerning this Notice should be directed to

Paul Mathews, Supervisor, Corporate Financing Department at (202) 728-8258.

Text of Proposed Amendment to Article III, Section 44 of the Rules of Fair Practice

(Note: Proposed language is underlined.)

(c) Underwriting Compensation and Arrangements

(c)(1) - (c)(6)(B)(vi)(7) - no change

(8) Contains anti-dilution provisions designed to provide the underwriter and related persons with disproportionate rights, privileges and economic benefits which are not provided to shareholders or the purchasers of the securities offered to the public.

NASD NOTICE TO MEMBERS 93-11

SEC Grants OTC Bulletin Board® Interim Designation As a “Qualifying Electronic Quotation System”

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On December 30, 1992, the Securities and Exchange Commission (SEC) granted the NASD's request for interim designation of the OTC Bulletin Board® service (OTCBB) as a “Qualifying Electronic Quotation System” (QEQ System) for purposes of certain SEC Penny Stock Disclosure Rules that became effective on January 1, 1993. This designation will facilitate broker/dealer compliance with the new penny stock disclosure rules. Specifically, the QEQ System designation now permits broker/dealers to use inside quotations displayed in the OTCBB to: determine from the inside bid whether the stock is priced under \$5 and is therefore a “penny stock” as defined by Rule 3a51-1 of the Securities Exchange Act of 1934 (Exchange Act); provide the bid/ask quotation disclosures to customers required by Exchange Act Rule 15g-3; and determine the market value of the penny stocks for customers' monthly or quarterly account statements as required by Exchange Act Rule 15g-6.

SEC Penny Stock Disclosure Rules Summary

The SEC Penny Stock Disclosure Rules were adopted in April 1992 pursuant to the requirements of the *Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (Penny Stock Reform Act)*. The *Penny Stock Reform Act* was enacted to require more stringent regulation of broker/dealers that recommend penny stock transactions to customers, and to promote the establishment of a structured electronic marketplace for dealers to quote such securities. The rules require a broker/dealer that has recommended a transaction to a customer in a “penny stock” as

defined by the Rules to provide that customer with certain specified information. In general, a penny stock is defined as a non-Nasdaq® and non-exchange-listed equity security, currently priced under \$5 per share, that is issued by a company with *less* than a specified amount of net tangible assets, continuous operations, or annual revenues.

Unless the transaction is exempt under the Rules, broker/dealers effecting customer transactions in such defined penny stocks are required to provide their customers with: a risk disclosure document; disclosure of the current inside bid and ask quotations, if any; disclosure of compensation to the broker/dealer and its salesperson in the transaction; and monthly or quarterly account statements showing the market value of each penny stock held in the customer's account. Several categories of penny stock transactions are exempt under Exchange Act Rule 15g-1, including transactions where the customer is an “institutional accredited investor” or customer transactions not recommended by the broker or dealer. The Rule 15g-2 requirement for the delivery of the risk disclosure document to penny stock customers became effective July 15, 1992. The other disclosure requirements became effective on January 1, 1993. (See *Notice to Members 92-38* July 1992.)

OTCBB Inside Quotations Use

Presently, the OTCBB calculates and displays an inside bid and ask for all securities with at least two registered market makers displaying firm, two-sided quotations.

Interim designation of the OTCBB as a QEQ System for purposes of the Penny Stock Disclosure Rules

permits member firms to use inside bid quotations for stocks displayed on the OTCBB to determine whether they should be classified as a penny stock. Essentially, Rule 3a51-1 defines a penny stock as any non-Nasdaq and non-exchange-listed security currently priced at less than \$5 per share and issued by a company not having certain prescribed net tangible assets, continuous operations, or annual revenues. The inside bid quotation on the OTCBB for the security is one method to determine that price.

This interim designation as a QEQ System will facilitate compliance with the bid and ask quotation disclosure requirement (Rule 15g-3) and the monthly/quarterly account statement requirement (Rule 15g-6) also will be significantly facilitated. Broker/dealers may use the inside bid and offer quotation displayed on the OTCBB for a penny stock to make disclosures required by these rules.

Specifically, SEC Rule 15g-3 requires broker/dealers — before executing a penny stock transaction with a customer — to disclose to that customer the current inside bid and offer quotations or similar market information regarding the penny stock. This disclosure also must be provided at the time of the trade.

Members are cautioned, however, that disclosure of the OTCBB inside bid and ask quotation for a penny stock does not permit such quotations to be used as the best evidence of the prevailing market for markup or markdown purposes without proper validation of the quotes. (For more details about validation of quotations, see *Notice to Members 92-16* April 1, 1992.)

SEC Rule 15g-6 requires broker/dealers that have sold penny stocks to customers in transactions

not exempt under Rule 15g-1 to send those customers (within 10 days after the end of the month or quarter) monthly or quarterly account statements. The statements must include the penny stock issuer's name, the number of shares, and the estimated market value as of the end of the month or quarter covered. That estimated market value should be, if available, the "highest inside bid quotation" for the penny stock on the last trading day of the period to which the statement relates, multiplied by the number of shares or units of the security in the customer's account.

Designation of the OTCBB as a QEQ System facilitates members' compliance efforts with the new Penny Stock Disclosure Rules by permitting the use of OTCBB displayed inside bid/ask quotation. This benefit is only available for penny stocks quoted in the OTCBB since it is the only SEC-designated QEQ System to date. For penny stocks not quoted on the OTCBB or where lack of market-maker quotations precludes the calculation of an inside market, member firms must undertake more burdensome procedures to make the price determinations necessary to satisfy the disclosure requirements contained in the Penny Stock Disclosure Rules.

Expected 17B Status for OTCBB

The *Penny Stock Reform Act* also requires the permanent establishment of a structured electronic marketplace for dealers to quote penny stocks. The NASD® views the QEQ System status for the OTCBB as an intermediate step in permanently achieving SEC recognition of the OTCBB as an automated quotation system under Exchange Act Section 17B. Section 17B directs the SEC to facilitate and oversee the creation

of one or more automated quotation systems for penny stocks with the following minimum characteristics: capacity to capture and display firm bids/offers entered by participating broker/dealers for individual securities; capacity to capture and display last-sale price and volume information for individual transactions reported by participating broker/dealers; ability to effect broad dissemination of participants' quotations and last-sale prices to broker/dealers and their customers; and sponsorship and regulation of the system by a national securities association or securities exchange. It should be emphasized that enactment of Section 17B reflects the Congress' intent to deter the fraudulent/manipulative trading practices chronicled in the *Penny Stock Reform Act's* legislative history. Often, those practices were facilitated by a lack of market transparency and reliable quotation and transaction price information for penny stocks. Hence, Congress mandated creation of an automated quotation system (or systems) to enhance the operation and regulation of dealer markets in penny stocks.

Presently, the OTCBB satisfies all requirements for Section 17B designation with the exception of collecting and disseminating trade reports on a real-time basis. However, the NASD has submitted a proposed rule change (File No. SR-NASD-92-48) to the SEC that would establish requirements for real-time reporting of members' transactions in penny stocks and other equity securities that may be quoted in the OTCBB or other inter-dealer quotation systems. At the same time, the NASD is developing the necessary system enhancements, which are expected to be implemented by mid-August. The OTCBB will then be eligible for permanent status as both a

Section 17B system as well as a qualifying system for purposes of the applicable penny stock regulations. Meanwhile, member firms are encouraged to maximize their use of the OTCBB for quoting markets in penny stocks (as defined by Exchange Act Rule 3a51-1) to take

advantage of the benefits of the OTCBB's interim designation as a QEQ System.

Questions concerning this Notice may be directed to Michael J. Kulczak of the NASD's Office of General Counsel at (202) 728-8811.

Compliance questions concerning the various penny stock regulations should be directed to Gary A. Carleton, Daniel M. Sibears, or William R. Schief of the NASD's Regulation staff at (202) 728-8959.

NASD NOTICE TO MEMBERS 93-12

Questions and Answers About New NASD® Rules Governing Investment Company Sales Charges — Article III, Sections 26(b) and (d) of the Rules of Fair Practice

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

Since the Securities and Exchange Commission (SEC) approved new NASD® rules governing investment company sales charges on July 7, 1992, the NASD has fielded numerous questions from member firms and mutual funds concerning the interpretation and application of these rules. In anticipation of the July 7, 1993, effective date of the new rules, the NASD has compiled in this Notice frequently asked questions and answers to help members understand and apply these rules. The categories addressed are calculation of sales charges and interest, retroactive calculation of remaining amounts, service fees, and exchanges.

Background

On July 7, 1992, the SEC approved amendments to Article III, Sections 26(b) and (d) of the Rules of Fair Practice (Rules) relating to investment company sales charges as announced in *Notice to Members 92-41* (August 1992). The new Rules take effect on July 7, 1993. The text of the new Rules follows this Notice. The following questions and answers have been developed to assist members in interpreting and implementing the new Rules.

The statements contained in this *Notice to Members* supersede and replace any and all prior statements of the NASD on the subject of investment company sales charges to the extent such prior statements are inconsistent with this Notice. The NASD may publish other question and answer Notices as needed to answer member questions.

Members are also reminded that, while Article III, Section 26 of the Rules of Fair Practice addresses

investment company issues, the Rules apply to members, not investment companies. Members are obligated under the Rule to ensure that the sales charges paid by the investment companies for the shares that they sell to the general public comply with the requirements of the Rules. A member that sells shares of an investment company in violation of the Rule is subject to disciplinary action, not the investment company. Nevertheless, members may rely on the statements in a fund's prospectus, or on statements from the fund about the amount of sales charges paid in the distribution of fund shares, unless the member knows, or should have known on the exercise of reasonable diligence, that the statements are not true.

Questions regarding this Notice may be directed to R. Clark Hooper, Vice President, Investment Companies at (202) 728-8329 and Elliott R. Curzon, Senior Attorney, Office of General Counsel at (202) 728-8451.

Questions and Answers

As an aid to understanding the questions and answers contained in this Notice, the NASD has developed a comprehensive example using a hypothetical investment company to show the calculations for remaining amount, balance for interest, and interest.¹ Readers are referred to this example on page 56

¹ Readers should note that for purposes of the calculations discussed in this Notice each class of shares and each series may be treated as a separate investment company. In *Notice to Members 90-56* (September 1990) requesting member vote on the new Rule the NASD stated that "[t]he Board considers each class of shares to be a separate investment company for purposes of the sales charge Rule."

for illustrations of the concepts described in this Notice.

I. Calculation of Sales Charges and Interest

Question #1: How often should a fund² with an asset-based sales charge calculate the remaining amount³ under its appropriate aggregate cap⁴ to which its total sales charges are subject for purposes of ensuring that it is in compliance with the limits under the Rules?

Answer: The remaining amount should be calculated at least as frequently as the fund makes payments of an asset-based sales charge, but in no event less frequently than once each calendar quarter. Thus, for example, a fund that pays an asset-based sales charge quarterly should calculate its remaining amount at least quarterly, and a fund that pays daily should calculate its remaining amount daily.

Question #2: How would a fund that pays asset-based sales charges quarterly make monthly calculations of its remaining amount (i.e., what happens when the fund's payment period is different from the period for which it calculates its remaining amount)? How should such a fund calculate interest?

Answer: The remaining amount would be calculated by multiplying the appropriate aggregate cap times new gross sales for the month, subtracting any front-end or deferred sales charges collected and any asset-based sales charges accrued during the month. The remaining amount for the month is then added to any pre-existing remaining amount and interest on the entire remaining amount is then calculated in the manner described in Questions 3 and 4.

A fund may also track a separate "balance for interest," which would be the appropriate aggregate cap times new gross sales for the period, minus any front-end, deferred, or asset-based sales charges collected during the period, and then added to any pre-existing "balance for interest." This new "balance for interest" (to which the prime rate, or an average of the prime rates for the period, plus one percent, would be applied) differs from the fund's remaining amount before interest as described above in that asset-based sales charges accrued but not paid would not be deducted. Thus, interest can be assessed on the amount represented by the accrued, but unpaid, asset-based sales charges. This difference in the balance used to calculate interest takes into account the fact that a fund underwriter that advances money to pay up front for distribution costs will not be reimbursed until the asset-based sales charge is actually paid to the underwriter.

Question #3: The Rules permit funds to increase their remaining amount by adding interest at the prime rate plus one percent. How and when should a fund determine the appropriate interest rate?

Answer: NASD *Notice to Members 90-56* (September 1990) describes the prime rate as "the most preferential rate of interest charged by the largest commercial banks on loans to their corporate clients" and refers to the rate published daily in *The Wall Street Journal*. Thus, the prime rate used for this purpose should be the rate appearing in *The Wall Street Journal*, which represents "the base rate on corporate loans posted by at least 75 percent of the nation's 30 largest banks." The prime rate in effect on the date when the fund calculates its remaining amount plus one percent (see Question 1) if the fund calculates

daily or, alternatively, if a fund calculates its remaining amount less frequently, an average of the prime rates over the period plus one percent should be used to calculate the amount by which a fund may increase its remaining amount. Funds generally should select and consistently use one of the above two alternatives.

Question #4: To calculate the increase in a fund's remaining amount based on the interest allowed (referred to in Question 3), to what amount should the prime rate plus one percent be applied?

Answer: Subparagraphs (d)(2)(A), (B), and (C) of Article III, Section 26 of the NASD Rules of Fair Practice refer to "interest charges

²The term "fund" as used in this Notice refers to open-end investment companies or single payment investment plans issued by a unit investment trust registered under the Investment Company Act of 1940.

³The term "remaining amount" as used in this Notice refers to the appropriate aggregate caps minus the amount of sales charges paid or accrued, including asset-based sales charges, front-end and deferred sales charges, plus the permitted interest. On the effective date of the new Rule, July 7, 1993, each fund will begin with either a zero remaining amount or a remaining amount calculated pursuant to new Subsection 26(d)(2)(C) on the basis of its historical sales and charges (see Question 11).

⁴The term "appropriate aggregate cap" refers to the appropriate maximum aggregate sales charge for the fund in question as specified in Subsection 26(d) of the new Rule. For a fund with an asset-based sales charge and a service fee (see Questions 18-26 with respect to service fees) the appropriate aggregate cap will be 6.25 percent of total new gross sales. For a fund with an asset-based sales charge and no service fee the appropriate aggregate cap will be 7.25 percent of total new gross sales.

on such amount,” and “such amount” is the appropriate aggregate cap on sales charges. As indicated in *Notice to Members 92-41* (August 1992), however, the NASD intended that interest be calculated not on the appropriate aggregate cap but rather on the fund’s remaining amount before the current interest calculation (i.e., the portion of the amount permitted to be charged that has not yet been paid). In calculating the permitted interest allowance, the fund should apply the appropriate interest rate (prime plus one percent) (see answer to Question 3) to its remaining amount or “balance for interest” (see discussion in answer to Question 2). For example, if a fund calculates its remaining amount daily, but pays asset-based sales charges monthly, it should apply the prime rate plus one percent to the current day’s “balance for interest.” If a fund calculates its remaining amount monthly and pays asset-based sales charges monthly, it should apply an average of the month’s prime rates plus one percent to its average remaining amount for the month. The NASD believes that if a fund adopts a particular method of accruing or paying charges and calculating its remaining amount and interest, it must consistently apply and adhere to the chosen practices. Funds may not change practices for short-term advantage to the distributor or underwriter.

Question #5: If a fund’s remaining amount reaches zero, what do the Rules require?

Answer: If a fund’s remaining amount reaches zero it must stop accruing asset-based sales charges and retain any deferred sales charges collected, until it has new sales that increase the remaining amount. In the NASD’s view, the prudent fund whose remaining amount is approaching zero should

calculate its remaining amount on a more frequent (even daily) basis so that it stops accruing asset-based sales charges when its remaining amount reaches zero.

The NASD is aware that in many cases front-end sales charges are paid directly to the selling member through deduction of the sales charge from the proceeds of sale; however, front-end sales charges deducted by the member will not exceed the remaining amount because each purchase will raise the remaining amount and the increase will not be consumed by the front-end sales charge.

Question #6: If a fund generates no sales or discontinues selling its shares, must it stop paying any asset-based sales charges?

Answer: No. The Rule provides only that the fund stop paying sales charges (either asset-based or deferred) when its remaining amount is depleted. A fund may fail to generate sales or stop selling its shares before its remaining amount is exhausted.

Question #7: For purposes of determining when a fund must begin to retain deferred sales charges because the remaining amount has been exhausted, must the fund determine on which day it exhausted the remaining amount?

Answer: The requirement that the fund retain deferred sales charges upon exhausting its remaining amount will be deemed to be met if the fund begins to retain those charges no later than the first day of the month following the month during which the remaining amount was depleted. As stated above, a fund should calculate its remaining amount more frequently as it approaches zero. In addition, a fund which has depleted its remaining

amount must also continue to retain deferred sales charges in subsequent months until its remaining amount becomes positive as a result of new sales. If an underwriter/distributor is collecting the deferred sales charges in such cases, it has an obligation to turn such amounts over to the fund immediately.

Question #8: If a fund’s remaining amount is depleted, so that it must stop accruing asset-based sales charges, and subsequently it has new sales which result in a positive remaining amount, can it resume accruing asset-based sales charges at a rate that, if annualized, would exceed .75 percent of its assets so long as the fund pays no more than .75 percent for the year?

Answer: No. It is contrary to the intent of the Rule for a member to sell the shares of a fund that on any given day has an asset-based sales charge in excess of .75 percent calculated on an annualized basis.

Question #9: If a fund has depleted its remaining amount and is retaining deferred sales charges, but subsequently has new sales that result in a positive remaining amount, can the underwriter recoup the deferred sales charges that were previously paid to the fund if the remaining amount increase occurs within the same fiscal period as exhaustion of the remaining amount?

Answer: No. Allowing the underwriter to recoup deferred sales charges paid to the fund in these circumstances is not consistent with the intent of the Rules.

Question #10: Can assets acquired through a statutory merger or a purchase of assets for shares be treated as new sales under the Rules?

Answer: No. But if a fund acquires a fund with an asset-based sales

charge and a remaining amount, the acquiring fund is permitted (not required) to add the acquired fund's remaining amount to its own remaining amount. Further, this remaining amount carry-over is not limited to funds with the same underwriter.

II. Retroactive Calculation of Remaining Amounts

Subparagraph 26(d)(2)(C) permits a fund to “look back” to sales which occurred before the effective date of the Rules to calculate its remaining amount as of the effective date of the Rules. The following questions and answers address issues related to the determination of a fund's starting balance.⁵

Question #11: Subparagraph (d)(2)(C) of Article III, Section 26 permits a fund to increase its remaining amount to take into account sales made between the time the fund first adopted an asset-based sales charge and July 7, 1993 (the effective date of the new provisions). How should a fund calculate the appropriate remaining amount as of that date?

Answer: To calculate its starting balance, a fund looks back to the date when it began paying an asset-based sales charge. It calculates the appropriate aggregate cap based on new gross sales from that date, subtracts actual sales charges paid or accrued from that date (including asset-based, front-end, and deferred) and adds interest as permitted under the Rules (see answer to Question 16). This amount is the fund's starting balance as of July 7, 1993. For purposes of this provision the NASD will deem a fund to have begun paying an asset-based sales charge only if it was actually paying the charge. A fund with an approved asset-based sales charge

which was never implemented (sometimes referred to as a “defensive 12b-1 Plan”) may not rely on this provision.

Question #12: Must a fund calculate its starting balance on the same basis as it will calculate its remaining amount after July 7, 1993?

Answer: No. A fund is not required to calculate its starting balance on the same basis as it will calculate its remaining amount after the new provisions take effect. This flexibility is intended to accommodate funds that, for example, may wish to do daily calculations going forward but might not have the ability to make daily calculations based on prior sales. Thus, notwithstanding the answer to Question 1, a fund need not make its retroactive calculations on the same or greater frequency as the fund paid asset-based sales charges.

Question #13: In determining the starting balance, may a fund with an asset-based sales charge exclude fees paid pursuant to a 12b-1 plan that meet the definition of “service fees” under the new NASD provisions from the required reduction representing actual sales charges paid?

Answer: Yes. As noted in Question 11, a fund is permitted to make these calculations as though the new provisions (including all definitions thereunder) had been in effect from the time an asset-based sales charge was adopted. Therefore, to the extent “service fees” (as defined in subparagraph (b)(9) of the amended Rules and discussed in Questions 17-25), whether or not separately described as service fees at the time, were actually paid by the fund, the amount of such fees not exceeding .25 percent may be excluded from the reduction representing asset-

based sales charges paid. The fund's records must be sufficiently detailed to identify payments of fees which meet the definition of service fees under the Rule. A fund is not permitted a “freebie” exclusion of .25 percent in the absence of documentary evidence that a service fee was actually paid. A fund that can establish that it paid a service fee should use the 6.25 percent aggregate cap in calculating its starting balance.

Question #14: In determining a fund's starting balance, which aggregate limit should be applied by a fund with an asset-based sales charge that did not pay a service fee before the effective date of the Rule but that will pay a service fee after the effective date of the Rule?

Answer: A fund that did not pay a service fee before the effective date may use the 7.25 percent limit to calculate its starting balance. As with the circumstances described in Question 13, a fund that paid a service fee as defined in the Rule may not opt to use the 7.25 percent limit by declining to declare that it paid such a service fee if its records show that it did. By the same reasoning, a fund that paid a service fee for only a portion of the prior period can apply the 7.25 percent limit for the portion of the period during which it did not pay a service fee.

Question #15: May a fund that, before the effective date of the new provisions, has had a 12b-1 plan limiting payments under the plan to a level lower than the new NASD aggregate limits, nonetheless, use the appropriate aggregate

⁵The term “starting balance” as used in this Notice means the remaining amount of the fund as of the effective date of the Rule calculated pursuant to new Subsection 26(d)(2)(C).

caps to calculate its starting balance?

Answer: Yes. The new Rules, however, do not amend a fund's 12b-1 plan and permit it to pay more than specified in the plan if such a plan has limits that are lower than the limits in the new Rules.

Question #16: If a fund calculates its starting balance without making interim (e.g., monthly, quarterly, etc.) calculations, how should the appropriate interest allowance be calculated?

Answer: A fund that calculates its starting balance based on new sales from the date of adopting an asset-based sales charge until the effective date of the amended Rules without making interim calculations should apply the average of the prime rates for the period, plus one percent, to an estimate of the average remaining amount over that period.

III. Service Fees

Question #17: What does the term "service fees" include or exclude?

Answer: The term "service fees" is defined in subparagraph (b)(9) of the amended Rules to mean "payments by an investment company for personal service and/or the maintenance of shareholder accounts."⁶ As noted in the explanatory section of NASD *Notice to Members 90-56* (September 1990), the term "service fees" is not intended to include transfer agent, custodian, or similar fees paid by funds. In addition, the phrase is not intended to include charges for the maintenance of records, record-keeping, and related costs. *Notice to Members 92-41* (August 1992) states that "service fees are intended to be distinguished from other

fees as a payment for personal service provided to the customer. It is essentially intended to compensate members for shareholder liaison services they provide, such as, responding to customer inquiries and providing information on their investments. It is not intended to apply to fees paid to a transfer agent for performing shareholder services pursuant to its transfer agent agreement. This fee does not include recordkeeping charges, accounting expenses, transfer costs, or custodian fees." Finally, the fact that a fund pays a fee pursuant to a "shareholder servicing" or similarly described plan does not conclusively determine whether the fee or any portion thereof constitutes a "service fee" for purposes of the Rules.

In broad categories the term does not include subtransfer agency services, subaccounting services, or administrative services. Specific services not covered by the term "service fee" include:

- Transfer agent and subtransfer agent services for beneficial owners of the fund shares.
- Aggregating and processing purchase and redemption orders.
- Providing beneficial owners with statements showing their positions in the investment companies.
- Processing dividend payments.
- Providing subaccounting services for fund shares held beneficially.
- Forwarding shareholder communications, such as proxies, shareholder reports, dividend and tax notices, and updating prospectuses to beneficial owners.
- Receiving, tabulating, and transmitting proxies executed by beneficial owners.

Question #18: How does a fund that pays a member a single fee for investment advisory, administrative, shareholder liaison, and other services comply with the limitation on service fees in the new Rule?

Answer: To comply with the Rule a member receiving such a fee pursuant to an omnibus servicing plan must identify those portions of the fee which are covered by the limitations of the Rule and ensure that the fees comply. There is no restriction on such fees in general, provided the member can demonstrate compliance with the Rule.

Question #19: Are service fee payments limited to .25 percent?

Answer: Yes. A fund may not pay more than .25 percent and treat such payments as service fees for purposes of the Rules. This applies whether payments are made directly by the fund or through the underwriter/adviser as a conduit. The new Rule does not apply to additional amounts paid by the underwriter or adviser out of its own resources. However, such additional amounts should not be called service fees.

Question #20: Can an underwriter/adviser take the .25 percent from the fund and reallocate it so that some dealers receive more and some less than .25 percent?

⁶The term "service fees," intended to describe payments that compensate members for providing personal service and maintenance of shareholder accounts, is being substituted for the previously used term "trail commission." The NASD believes the term "service fees" more accurately describes the intent of the payments and intends that the term "trail commission" not be used in the future to describe such payments.

Answer: No. This violates the intent of the Rule.

Question #21: Subparagraph (d)(5) imposes a limit on service fees paid to any member of .25 percent of the average annual net asset value of shares sold. Does this include shares acquired through reinvestments of distributions paid on shares sold by that member?

Answer: Yes. The NASD intended to have the limit apply to shares acquired through distribution reinvestments as well as shares actually sold.

Question #22: May a fund determine that it is in compliance with the limits on service fees by referring to the level of its net assets on the dates on which it calculates payments of service fees?

Answer: Yes. The fund should determine that it is in compliance with the limits on service fees that can be paid consistent with its method for calculating such fees. That is, a fund that uses a specific record date to calculate service fees should use its net assets on such date, while a fund that calculates fees based on average assets during a specific period should use the average net assets during such period (e.g., monthly or quarterly).

Question #23: Is there a clear distinction between asset-based sales charges and service fees?

Answer: Yes.

Question #24: If an item is a service fee, is it outside the scope of the Rule's limits on sales charges?

Answer: Yes.

Question #25: Is a fund's service fee counted as part of the 12b-1 fees?

Answer: Whether SEC Rule 12b-1 requires service fees to be included in a 12b-1 plan is not addressed by the NASD's Rule.⁷

IV. Exchanges

The following questions address exchanges or transfers between funds in the same family, and the transfer of a portion of a remaining amount corresponding to the amount exchanged. Notwithstanding the extensive discussion of exchanges, there is no obligation in the Rule to transfer any remaining amount.

Question #26: If Fund A chooses to increase its remaining amount based on exchanges from Fund B (a fund within the same complex), thus requiring the deduction of a corresponding amount from the remaining amount of Fund B, must Fund B treat exchanges from Fund A in the same manner?

Answer: Yes, except as provided in Question 30. This requirement will help ensure that inequities do not result as between the two funds.

Question #27: By what amount should Fund A increase its remaining amount based on exchanges from Fund B?

Answer: As indicated in NASD *Notice to Members 90-56* (September 1990), a fund may increase its remaining amount by treating the shares received through an exchange as new gross sales (if the amount of such increase is deducted from the remaining amount of the fund out of which shares are exchanged). However, funds may choose to transfer less than this maximum amount allowed pursuant to a fund policy that is consistently applied in accordance with Question 26. Funds may deter-

mine to transfer some portion of the remaining amount, rather than the maximum amount allowed, for a variety of reasons. For example, applying the applicable maximum sales charge to the exchanged shares to determine the amount of the increase in Fund A's remaining amount — as will be the case if exchanges are treated as new gross sales — does not take into account that asset-based sales charges already have been assessed on those shares or that they may have been in the original fund for some period of time, during which that fund's remaining amount was depleted.

Examples of policies that funds might adopt under which less than the maximum amount allowed of the remaining amount would be transferred include, but are not limited to: (1) a policy pursuant to which a percentage of Fund B's remaining amount that is the same as the percentage of net assets of Fund B being exchanged into Fund A is added to Fund A's remaining amount; (2) a policy under which a percentage less than the maximum appropriate aggregate cap, that takes into consideration the aging of the exchanged shares (e.g., 2 percent rather than 6.25 percent), is applied to the amount being transferred from Fund B to Fund A; or (3) a policy under which the applicable sales charge is multiplied by the value of the exchanged shares at the time of their original purchase (as opposed to their value at the time of the exchange) for purposes of determining the increase in Fund A's remaining amount.

⁷The SEC has stated that “[w]hether particular shareholder or other services are starting balance” as used in this Notice means the remaining amount of the fund as of the effective date of the Rule calculated pursuant to new Subsection 26(d)(2)(C).

Question #28: If Fund A, which has an asset-based sales charge, receives an exchange from Fund B, which does not have an asset-based sales charge (and, therefore, no “remaining amount” from which to deduct an increase in Fund A’s remaining amount) may it increase its remaining amount? This could occur, for example, where a fund complex uses a money market fund (Fund B) as the initial repository for investments which will thereafter be transferred periodically into an equity fund (Fund A) pursuant to a “dollar-cost averaging” program.

Answer: In this case Fund A could treat the amount exchanged as new gross sales for purposes of the Rule even though there is no “remaining amount” in Fund B from which to deduct Fund A’s increase. If Fund A does so, however, it should decrease its remaining amount on any exchange from Fund A to Fund B. This treatment would be the same whether the investor originally invested in Fund A directly or exchanged Fund B shares for Fund A shares.

Question #29: By what amount may a fund increase its remaining amount based on exchanges from a fund that has a front-end sales charge?

Answer: The fund into which shares are exchanged may increase its remaining amount by an amount that is no more than the appropriate aggregate cap, minus the other fund’s maximum front-end sales charge (but not in any event less than zero), times the amount being exchanged, in order to reflect appropriately the assessment of the initial sales charge. This requirement applies whether or not the front-end sales charge fund has an asset-based sales charge.

Question #30: What happens if the fund from which shares are being exchanged has already exhausted its remaining amount?

Answer: No remaining amount adjustments should be made in this instance as the underwriter/adviser has already received all monies due from the prior sale.

Question #31: What happens if an exchange is made from a fund that has not exhausted its remaining balance to one that has?

Answer: If the fund’s general policy on exchanges calls for the transfer of remaining amounts, then an appropriate amount may be transferred between the two funds.

Question #32: How are exchanges before the effective date of the Rule amendments treated?

Answer: A fund may treat these exchanges in any manner that would be permitted for exchanges occurring after the amendments become effective (including choosing not to make any adjustments based on exchanges), as long as any method chosen is applied consistently for the entire period.

Question #33: Can different funds within the same fund complex have different policies regarding exchanges?

Answer: Yes, as long as each fund treats exchanges into it from any other fund the same as that other fund treats exchanges from the first fund, as set forth in Question 26 (subject to the exception described in Question 30 concerning funds that have exhausted their remaining amounts). Thus, a fund’s policy regarding treatment of exchanges may differ depending on the fund from which the exchange comes or to which it goes.

V. Miscellaneous

Question #34: May a particular class of securities within a given portfolio of a fund be referred to as a “no load” class, provided that the particular class has no front-end or deferred sales charges, and has no asset-based sales charges and/or service fees aggregating more than .25 percent, but where other classes of securities within the same portfolio do have front-end or deferred sales charges or asset-based fees in excess of .25 percent?

Answer: Yes. *Notice to Members 90-56* (September 1990) requesting member vote on the new Rule stated “[t]he Board considers each class of shares and each series to be a separate investment company for purposes of the sales charge Rule.”

Question #35: The NASD’s Rule separately defines asset-based sales charges and service fees. How should a fund that pays both asset-based sales charges and service fees pursuant to a Rule 12b-1 plan make disclosure that complies with the SEC’s Form N-1A, and at the same time make clear that the fund is complying with the NASD’s Rule?

Answer: Form N-1A requires adequate disclosure of fees paid and charges imposed by a mutual fund. While the NASD does not take a position on the adequacy of disclosures in Forms N-1A, either in general or in specific cases, in many cases the principal source of information for a member firm for such fees will be the prospectus. Funds would be well advised to include prospectus disclosure regarding the fees paid and charges imposed in a manner sufficient for member firms to prove that they can sell the fund’s shares in compliance with the NASD’s Rules.

Comprehensive Example Showing Remaining Amount, Balance for Interest, and Interest Calculations

		Remaining Amount	Balance for Interest
		0	0
Balance forward from prior calculation			
New gross sales for month	10,000,000		
Appropriate aggregate cap	6.25%	625,000	625,000
Deferred sales charges collected for month		(10,000)	(10,000)
Asset-based sales charges accrued for month		(3,000)	
Asset-based sales charges paid during month			0
Balance before interest		612,000	615,000
Interest calculation:			
Average balance for interest			
{(Beginning + ending)/2}	307,500		
Interest rate (average prime + 1%)/12	0.5833%	1,794	1,794
Balance at end of month 1		613,794	616,794
New gross sales for month	20,000,000		
Appropriate aggregate cap	6.25%	1,250,000	1,250,000
Deferred sales charges collected for month		(45,000)	(45,000)
Asset-based sales charges accrued for month		(12,000)	
Asset-based sales charges paid during month			0
Balance before interest		1,806,794	1,821,794
Interest calculation:			
Average balance for interest			
{(Beginning + ending)/2}	1,219,294		
Interest rate (average prime + 1%)/12	0.5833%	7,113	7,113
Balance at end of month 2		1,813,906	1,828,906
New gross sales for month	20,000,000		
Appropriate aggregate cap	6.25%	1,250,000	1,250,000
Deferred sales charges collected for month		(60,000)	(60,000)
Asset-based sales charges accrued for month		(24,000)	
Asset-based sales charges paid during month			(39,000)
(Equals 3 months accrued)			(39,000)
Balance before interest		2,979,906	2,979,906
Interest calculation:			
Average balance for interest			
{(Beginning + ending)/2}	2,404,406		
Interest rate (average prime + 1%)/12	0.5833%	14,026	14,026
Balance at end of month 3		2,993,932	2,993,932

Assumptions used:

- * Fund has a service fee, therefore appropriate aggregate cap = 6.25 percent.
- * Fund calculates remaining balance monthly, based on aggregate data for month.
- * Fund pays asset-based sales charges at end of quarter.
- * Prime rate was 6 percent for entire period.

Text of Section 26 of the Rules of Fair Practice Reflecting Amendments Approved By the SEC in SR-NASD-91-61

Investment Companies

Sec. 26

* * * * *

Definitions

(b)

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(4) Person shall mean "person" as defined in the Investment Company Act of 1940.

* * * * *

(8) "Sales charge" and "sales charges" as used in subsection (d) of this section shall mean all charges or fees that are paid to finance sales or sales promotion expenses, including front-end, deferred and asset-based sales charges, excluding charges and fees for ministerial, recordkeeping or administrative activities and investment management fees. For purposes of this section, members may rely on the sales-related fees and charges disclosed in the prospectus of an investment company.

(A) A "front-end sales charge" is a sales charge that is included in the public offering price of the shares of an investment company.

(B) A "deferred sales charge" is a sales charge that is deducted from the proceeds of the redemption of shares by an investor, excluding any such charges that are (i) nominal and are for services in connection with a redemption or (ii) to discourage short-term trading, that are not used to finance sales-related expenses, and that are credited to

the net assets of the investment company.

(C) An "asset-based sales charge" is a sales charge that is deducted from the net assets of an investment company and does not include a service fee.

(9) "Service fees" as used in subsection (d) of this section shall mean payments by an investment company for personal service and/or the maintenance of shareholder accounts.

(10) "Prime rate" as used in subsection (d) of this section shall mean the most preferential interest rate on corporate loans at large U.S. money center commercial banks.

* * * * *

Sales Charges

(d) No member shall offer or sell the shares of any open-end investment company or any "single payment" investment plan issued by a unit investment trust (collectively "investment companies") registered under the Investment Company Act of 1940 if the sales charges described in the prospectus are excessive. Aggregate sales charges shall be deemed excessive if they do not conform to the following provisions:

(1) Investment Companies Without an Asset-Based Sales Charge

(A) Front-end and/or deferred sales charges described in the prospectus which may be imposed by an investment company without an asset-based sales charge shall not exceed 8.5% of the offering price.

(B)(i) Dividend reinvestment may be made available at net asset value per share to any person who requests such reinvestment.

(ii) If dividend reinvestment is not made available as specified in subparagraph (B)(i), the maximum aggregate sales charge shall not exceed 7.25% of the offering price.

(C)(i) Rights of accumulation (cumulative quantity discounts) may be made available to any person in accordance with one of the alternative quantity discount schedules provided in subparagraph (D)(i) below, as in effect on the date the right is exercised.

(ii) If rights of accumulation are not made available on terms at least as favorable as those specified in subparagraph (C)(i) the maximum aggregate sales charge shall not exceed:

(a) 8% of offering price if the provisions of subparagraph (B)(i) are met; or

(b) 6.75% of offering price if the provisions of subparagraph (B)(i) are not met.

(D)(i) Quantity discounts, if offered, shall be made available on single purchases by any person in accordance with one of the following two alternatives:

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

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

(ii) If quantity discounts are not made available on terms at least as favorable as those specified in subparagraph (D)(i) the maximum aggregate sales charge shall not exceed:

(a) 7.75% of the offering price if the provisions of subparagraphs (B)(i) and (C)(i) are met.

(b) 7.25% of the offering price if the provisions of subparagraph (B)(i) are met but the provisions of subparagraph (C)(i) are not met.

(c) 6.50% of the offering price if the provisions of subparagraph (C)(i) are met but the provisions of subparagraph (B)(i) are not met.

(d) 6.25% of the offering price if the provisions of subparagraphs (B)(i) and (C)(i) are not met.

(E) If an investment company without an asset-based sales charge pays a service fee, the maximum aggregate sales charge shall not exceed 7.25% of the offering price.

(F) If an investment company without an asset-based sales charge reinvests dividends at offering price, it shall not offer or pay a service fee unless it offers quantity discounts and rights of accumulation and the maximum aggregate sales charge does not exceed 6.25% of the offering price.

(2) Investment Companies With an Asset-Based Sales Charge

(A) Except as provided in subparagraphs (2)(C) and (2)(D), the aggregate asset-based, front-end and deferred sales charges described in the prospectus which may be imposed by an investment company with an asset-based sales charge, if the investment company has adopted a plan under which service fees are paid, shall not exceed 6.25% of total new gross sales (excluding sales from the reinvestment of distributions and exchanges of shares between investment companies in a single complex, between classes of shares of an investment company with multiple classes of shares or

between series shares of a series investment company) plus interest charges on such amount equal to the prime rate plus one percent per annum. The maximum front-end or deferred sales charge resulting from any transaction shall be 6.25% of the amount invested.

(B) Except as provided in subparagraphs (2)(C) and (2)(D), if an investment company with an asset-based sales charge does not pay a service fee, the aggregate asset-based, front-end and deferred sales charges described in the prospectus shall not exceed 7.25% of total new gross sales (excluding sales from the reinvestment of distributions and exchanges of shares between investment companies in a single complex, between classes of shares of an investment company with multiple classes of shares or between series shares of a series investment company) plus interest charges on such amount equal to the prime rate plus one percent per annum. The maximum front-end or deferred sales charge resulting from any transaction shall be 7.25% of the amount invested.

(C) The maximum aggregate sales charge on total new gross sales set forth in subparagraphs (2)(A) and (B) may be increased by an amount calculated by applying the appropriate percentages of 6.25% or 7.25% to total new gross sales which occurred after an investment company first adopted an asset-based sales charge until July 7, 1993, plus interest charges on such amount equal to the prime rate plus one percent per annum less any front-end, asset-based or deferred sales charges on such sales or net assets resulting from such sales.

(D) The maximum aggregate sales charges of an investment company in a single complex, a class of shares issued by an investment

company with multiple classes of shares or a separate series of a series investment company, may be increased to include sales of exchanges shares provided that such increase is deducted from the maximum aggregate sales charges of the investment company, class or series which redeemed the shares for the purpose of such exchanges.

(E) No member shall offer or sell the shares of an investment company with an asset-based sales charge if:

(i) The amount of the asset-based sales charge exceeds .75 of 1% per annum of the average annual net assets of the investment company, or

(ii) Any deferred sales charges deducted from the proceeds of a redemption after the maximum cap described in subparagraphs (2)(A), (B), (C), and (D) has been attained are not credited to the investment company.

(3) No member or person associated with a member shall, either orally or in writing, describe an investment company as being "no load" or as having "no sales charge" if the investment company has a front-end or deferred sales charge or whose total charges against net assets to provide for sales related expenses and/or service fees exceed .25 of 1% of average net assets per annum.

(4) No member or person associated with a member shall offer or sell the securities of an investment company with an asset-based sales charge unless its prospectus discloses that long-term shareholders may pay more than the economic equivalent of the maximum front-end sales charges permitted by this section. Such disclosure shall be adja-

cent to the fee table in the front section of a prospectus.

(5) No member or person associated with a member shall offer or sell the securities of an investment company if the service fees paid by the investment company, as disclosed in the prospectus, exceed .25 of 1%

of its average annual net assets or if a service fee paid by the investment company, as disclosed in the prospectus, to any person who sells its shares exceeds .25 of 1% of the average annual net asset value of such shares.

NASD NOTICE TO MEMBERS 93-13

Market-Maker Display of Size in Nasdaq Small- Cap MarketSM Securities

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

Effective February 1, 1993, market makers in Nasdaq Small-Cap MarketSM securities had to display size in their quotations of at least 500 shares, unless the issues are priced at \$10 or more and trade less than 1,000 shares per day. Those issues will remain at the 100 share-display requirement. The list of 100-share Small-Cap securities follows this Notice.

Discussion

The Securities and Exchange Commission (SEC) approved an amendment to Schedule D of the NASD By-Laws requiring market makers in Nasdaq Small-Cap Market securities to display size in their quotations equal to the 500-share maximum order size in SOES. The amendment became effective February 1, 1993. To preserve market-maker participation and liquidity in more expensive, less-frequently traded Nasdaq Small-Cap issues, however, the NASD has determined that Nasdaq Small-Cap equity securities that have a bid price of \$10 or more and an average daily non-block volume of less than 1,000 shares will remain with a 100-share display requirement. In Nasdaq Small-Cap issues that fall under these thresholds, market makers will have to continue posting size of a normal unit of trading. Although the size-display requirement for these issues will be 100 shares, market makers voluntarily participating in SOES should be aware that their tier-level and maximum-order size in SOES will remain at 500 shares. Nasdaq convertible debt securities are also exempt from the new size-display requirements.

The list of those Nasdaq Small-Cap securities with a 100-share display

requirement follows this Notice and the NASD will periodically (approximately every six months) review and analyze the trading characteristics of Nasdaq Small-Cap securities, including share price and average volume in the stock, to determine whether to modify the share requirements and will publish a *Notice to Members* regarding any modifications.

Questions concerning this Notice may be directed to Richard Bush, Nasdaq Operations, at (212) 858-4420.

Nasdaq Small-Cap Issues With Average Non-Block Volume Less Than 1,000 Shares and the Price Greater Than or Equal to \$10

Symbol	Company Name
FBCV	1st Bncp (IN)
AFINP	Amer Fin Cp Pfd D
AMPLP	Ampal Am Isrl 6.5 Pfd
ADWC	Ansonia Derby Water
APOL	Apollo Sav Loan Co
BONEP	Banc One Cp Pfd B
EATN	Bank of East Tenn
BKSC	Bank of South Carolina
BIRDP	Bird Cp 1.85 Pfd
CPXLU	C A P X Cp Uts (Del)
CBTC	C B T Cp
CSKKY	C S K Cp ADR
CAMTU	Car Mart Inc Uts 95
CAFCP	Carolina First Pfd
CTRL	Chemi Trol Chem
CLEA	Chemical Leaman Inc
CFCP	Coastal Fin Cp
CCPI	Comcast Cablevision
CFFC	Community Fed Sav
BPWRF	Compania Boliviana
CAIRP	Conquest Air Pfd A
DAIEY	Dai Ei Inc ADR
DKBC	Dakota Bancorp SE
DTUN	Detroit Canada Tunnel
ESBK	Elmira Sav Bk FSB
XTONP	Executone Cv Pfd A
FBANP	F N B Cp Conv Pfd B
FGNO	Fair Grounds Cp
FFII	Falls Financial Inc

Symbol	Company Name	Symbol	Company Name	Symbol	Company Name
FFKT	Farmers Capital Bank	JCFSP	Jackson Cnty Bk Pfd A	PINN	Pinnacle Banc Grp Inc
FNIN	Financial Inds	JFFNP	Jefferson Bk Pfd E	PRFB	Prime Federal Bank
FBPC	First Fin Bkshs Polk	WILLB	John Wiley Sons Cl B	RBSI	Regency Bcshs
FRCCP	First Fin Cari Pfd A	KIDD	Kiddie Products Inc	RLIFA	Reliable Life Ins Cl A
FPRY	First Fin Bncp Inc	KNBWY	Kirin Brewery Co	RSRFP	Riser Foods A Pfd Inc
FFSX	First FSB Siouxland		ADR	SLAB	Sage Labs Inc
FLIC	First of Long Island	LAUR	Laurel Bancorp Inc	SANYY	Sanyo Elec Co ADR
FUSB	First United Sav Bk	LARL	Laurel Savings Assoc	SAVB	Savannah Bncp Inc
FCVG	Firstfed Northern KY	LGASP	Louisville Pfd 5	STBC	State Bancorp Inc
GTELO	G T E Ca 4.5 Pfd	LGASO	Louisville Pfd 745	SFSW	State Fin Svcs Cl A
GTELP	G T E Ca 56 Pfd	MRNCZ	Marina Ltd Ptnr Uts	TENB	Tennessee Nat'l Bank
GAMBY	Gambro A B B ADR	MARPS	Marine Petroleum SBI	TNELB	Thomas Nelson Inc
GLDFY	Gold Field S So Africa	MFCNP	Metro Fin Pfd B		Cl B
GWOX	Goodheart Willcox	MFCNU	Metropolitan Fin Uts	TIRZC	Tidelands Royal Tr B
GCOM	Gray Comm Sys Inc	NSFC	Northern States Fin	UPCPN	Union Planter Pfd C
GAMI	Great Amer Mgmt Inv	NWNGP	Northwest Nat Gas Pfd	UCTC	United Counties Bncp
GYRO	Gyrodyne Co Amer	OCENY	Oce Van Grinten ADR	URIXU	Uranium Res Uts
TDXC	Health Mgmt Int'l Inc	OLDRP	Old Republic Cp Pfd E	VAFD	Valley Fed Sav Bk Al
HFLM	Hydro Flame Cp	OMEGU	Omega Environ Uts	VMRXU	Vimrx Pharm Inc Uts
IICR	I I C Inds Inc	PNCFP	P N C Fin Cp Pfd A	WACLY	Wacoal Cp ADR
IMTUC	Info Mgmt Tech Uts S2	PANRA	Panhandle Royal Cl A	WASH	Washington Trust
INVSP	Investors Sav Pfd	PNNW	Pennichuck Cp		

NASD NOTICE TO MEMBERS 93-14

Nasdaq National Market®
Additions, Changes,
And Deletions as of
January 21, 1993

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

As of January 21, 1993, the following 22 issues joined the Nasdaq National Market,® bringing the total number of issues to 2,970:

Symbol	Company	Entry Date	SOES Execution Level
INFU	Infu-Tech, Inc.	12/22/92	1000
TTRR	Tracor, Inc.	12/22/92	500
TTRRW	Tracor, Inc. (Ser A) (Wts 12/31/01)	12/22/92	500
WAMUO	Washington Mutual Sav Bk (Ser C) (Pfd) (Noncum)	12/22/92	500
WAMUN	Washington Mutual Sav Bk (Pfd) (Ser D)	12/22/92	200
TUTR	TRO Learning, Inc.	12/23/92	1000
ULBI	Ultralife Batteries, Inc.	12/23/92	1000
FNSC	Financial Security Corp.	12/29/92	1000
KNKB	Kankakee Bancorp, Inc.	1/6/93	1000
ARCI	Appliance Recycling Centers of America, Inc.	1/8/93	1000
SKIL	Canterbury Educational Services, Inc.	1/8/93	1000
CRTQ	Cortech, Inc.	1/8/93	1000
CRTQR	Cortech, Inc. (Rts) 5/24/94	1/8/93	1000
LIPOZ	Liposome Company, Inc. (The) (Dep) (Shrs)	1/8/93	500
AMCRY	AMCOR Limited ADR	1/11/93	1000
CMVT	Comverse Technology, Inc.	1/19/93	1000
COSI	Computer Outsourcing Services, Inc.	1/20/93	500
FIRE	Financial Institutions Insurance Group, Ltd.	1/20/93	200
HAHN	Hahn Automotive Warehouse, Inc.	1/20/93	1000
AIMM	AutoImmune Inc.	1/21/93	500
CHMP	Champion Industries, Inc.	1/21/93	1000
GNCI	General Nutrition Companies, Inc.	1/21/93	1000

Nasdaq National Market Symbol and/or Name Changes

The following changes to the list of Nasdaq National Market securities occurred since December 23, 1992:

New/Old Symbol	New/Old Security	Date of Change
TSLH/TCOR	TSL Holdings Inc./Tandon Corp.	12/24/92
ABBK/ABBK	Abington Savings Bank/Abington Bancorp Inc.	12/30/92
TDMK/NNSL	TideMark Bancorp Inc./Newport News Savings Bank	1/4/93
AFWY/AFWY	American Freightways Corp./Arkansas Freightways Corp.	1/4/93
BULL/BULL	Bull Run Corporation/Bull Run Gold Mines, Ltd.	1/6/93
SCSL/SCSL	Suncoast Savings & Loan Association, FSA/Suncoast Savings & Loan Assn.	1/8/93
CFIB/CFIB	CFI Industries, Inc./Consolidated Fibres Inc.	1/14/93
BEEF/QRXI	Western Beef Inc./Quarex Industries, Inc.	1/15/93

Nasdaq National Market Deletions

Symbol	Security	Date
AESM	Aero Systems, Inc.	12/22/92
HERC	Hadson Energy Resources Corporation	12/22/92
MDCOR	Marine Drilling Co. (Rts)	12/22/92
PHBKR	Peoples Heritage Financial Group Inc. (Rts)	12/22/92
SMBX	Symbolics, Inc.	12/22/92
AMFS	American Funeral Services Corp.	12/23/92
CMIKA	Carmike Cinemas Inc. (Cl A)	12/24/92
CBLMW	CBL Medical Inc. (Wts) 12/21/93	1/4/93
CHPK	Chesapeake Utilities Corporation	1/4/93
FSCB	First Commercial Bancshares Inc.	1/4/93
HMTB	HomeTrust Bank of Georgia	1/4/93
HFOX	Ultra Bancorp	1/4/93
NWRK	Networks Electronic Corp.	1/5/93
ACHV	Archive Corp.	1/6/93
HOSEE	Sheffield Industries, Inc.	1/6/93
CRTQZ	Cortech Inc. (Uts) 1994	1/8/93
EVRQE	Everex Systems, Inc.	1/12/93
PISC	Pacific International Services Corp.	1/12/93
GIES	Green Isle Environmental Services, Inc.	1/13/93
UAHC	United American Healthcare Corporation	1/14/93
ATPH	Armstrong Pharmaceuticals, Inc.	1/15/93
PSNB	Puget Sound Bancorp	1/15/93
DFSE	DFSoutheastern, Inc.	1/18/93
HBCI	Harmonia Bancorp Inc.	1/18/93
ITGR	Integra Financial Corporation	1/18/93
SCFB	South Carolina Federal Corp.	1/18/93
ARIXE	ARIX Corporation	1/20/93
GLGVF	Glamis Gold Ltd.	1/20/93
GHVI	Genesis Health Ventures, Inc.	1/21/93

Questions regarding this Notice should be directed to Mark A. Esposito, Supervisor, Market Listing Qualifications, at (202) 728-8002. Questions pertaining to trade-reporting rules should be directed to Bernard Thompson, Assistant Director, NASD Market Surveillance, at (301) 590-6436.

NASD BOARD BRIEFS

Actions Taken by the NASD Board of Governors in January

• **President's Report** — The Nasdaq Stock MarketSM set all-time highs in 1992 in share and dollar trading volume, the performance of its composite index, dollar volume of initial public offerings (IPOs), and dollar trading volume of foreign shares and American Depository Receipts (ADRs). Nasdaq's record-setting performance clearly positions it as the second largest stock market in the world as measured by dollar volume of trading.

The Nasdaq Stock Market remained the fastest growing equity market in the U.S., with a 17.3 percent rise in share volume to 48.5 billion. On 86 out of 254 trading days this year, Nasdaq[®] volume exceeded that of the New York Stock Exchange. The Nasdaq Composite closed out the year at a record high of 676.95—up 15.5 percent. Combined with 1991's increase, the Composite has soared more than 81 percent during the past two years. This exceptional market performance greatly helps Nasdaq companies raise new capital cost effectively.

The NASD[®] remains financially sound as revenues continued to exceed expenses with a healthy surplus anticipated for 1993. In a move to improve service to customers and accountability for corporate goal achievement, the NASD has realigned its structure into a customer-driven organization constructed around three business groups, Regulation, Market Services, and Member Services, supported by the Corporate Services and Technology Services Groups, with an Infrastructure Group underlying all five. The Infrastructure group includes the NASD's Governing and Advisory Boards as well as its Standing Committees and the Office of the President.

With the new administration and Congress convening, legislative action on securities matters can be expected. Because Congress must amend the Government Securities Act to restore the Treasury Department's authority to write government securities rules, the Government Securities Acts amendments will most likely be reintroduced early in the 103rd Congress. In the last Congress, the House and Senate were unable to resolve their differences on investment adviser legislation, which died when Congress adjourned. Given the effort spent on the bills by both Houses and the SEC's continuing need for more frequent investment adviser inspections, Congress is likely to reconsider investment adviser legislation. Notwithstanding the NASD's proposed partnership rollup rules, the new Congress will likely reconsider rollup legislation during this term.

• **Market Services** — A Code of Procedure amendment approved by the Board would permit the Nasdaq Hearing Review Committee to dismiss as abandoned certain appeals by Nasdaq issuers of decisions of the Nasdaq Listing Qualification Committee. Such dismissals would include appeals where the party seeking review fails to advise the Nasdaq Hearing Review committee of the reason for the review or otherwise fails to provide information in response to a request. This provision parallels procedures governing appeals of disciplinary matters to the National Business Conduct Committee.

Board-approved changes to Part III, Schedule D would add a bid price requirement for entry and maintenance under Alternative 2 of the existing Nasdaq National Market criteria. The proposal, which has to be filed with the SEC, provides for a minimum bid price of \$3 under

Alternative 2, and a minimum bid price of \$1 (or in the alternative, a market value of public float of \$3 million and \$4 million of capital and surplus) for continued designation.

Circumvention of Nasdaq listing criteria is the target of a proposed change to Schedule D approved by the Board. Under the proposal, the surviving company of a reverse merger would have to comply with Nasdaq initial inclusion requirements where there has been a change of control and a change in business or a change in the financial structure of the surviving company. The amendment addresses the problem of “backdoor listing” where a Nasdaq company, failing to meet the new, more stringent maintenance requirement, tries to sell its Nasdaq listing to a private company. The surviving company then becomes listed on Nasdaq without having had to go public, make public disclosures, or meet Nasdaq’s initial inclusion requirements.

The Board approved for filing with the SEC procedures for a change to the pre-opening application in the Intermarket Trading System/Computer Assisted Execution System (ITS/CAES) Rule. A market maker that intends to open an exchange-listed security outside the applicable price-change parameters at a price more than either 1/8 point or 1/4 point (depending on the price of the stock) away from the previous day’s consolidated closing price, must notify other participant markets of that fact by sending a pre-opening notification through ITS which also indicates the range of opening prices. Under the current rule language, a cancellation message sent subsequent to the pre-opening notification indicates that the stock will be opened within the applicable price-change parameters, but outside the range contained in

the original notification. The rule change provides that a cancellation notification shall be sent after a pre-opening notification whenever the stock will open within the applicable price-change parameters, irrespective of whether the opening price is within the range specified in the original notification.

The Board authorized publication of a Notice to remind members of their obligations under Section 66 of the Uniform Practice Code. Section 66 requires syndicate members to settle syndicate accounts within 90 days of the syndicate settlement date. In the NASD’s view, compliance with Section 66 mandates that syndicate managers mail, or, when appropriate, deliver checks to syndicate participants no later than the 90th day following settlement of the syndicate account. The NASD Operations Committee may, if the circumstances of a particular case warrant it, grant an exemption from these provisions.

Movement toward full book-entry settlement of securities transactions among financial institutions took a step closer with Board approval of a proposed rule requiring members to use the facilities of a securities depository for the book-entry settlement of all transactions between financial intermediaries in securities included in securities depositories. The proposed rule would not apply to transactions settled outside of the United States; transactions where a member cannot deposit the securities before the depository’s cut-off time for cash trades settling on the same day; and transactions where the deliverer cannot deposit the securities before the cut-off date set for the particular issue of securities involved in a tender offer or other reorganization.

• **Regulation** — The NASD will publish shortly a *Notice to*

Members addressing the issues related to the NASD’s new rules governing investment company sales charges. The Notice, in question and answer format, will provide interpretive advice to members on implementing the new rules. The Notice is divided into five sections:

- Calculation of sales charges and interest.
- Retroactive calculation of remaining amounts.
- Service fees.
- Exchanges.
- Miscellaneous.

To assist members in understanding the questions and answers, the Notice includes an example using a hypothetical investment company to illustrate the calculation referred to in the body of the Notice.

• **Member Services** — A proposal to expand the scope of the NASD Public Disclosure Program received the Board’s approval. As a result, the NASD will file changes with the SEC that would permit disclosure of civil judgments and arbitration decisions involving securities matters reported to the Central Registration Depository (CRD) on Forms U-4 and U-5; pending formal disciplinary proceedings initiated by the SEC, states, and self-regulatory organizations; and criminal indictments and information. The NASD is of the view that these matters are available to the public in one or more forums and therefore are appropriate for disclosure through the NASD’s programs. Any disclosures of criminal indictment and information, however, would be labeled to indicate the unadjudicated nature of the proceedings in the written disclosure documents sent to investors.

• **Advisory Council Recommendations** — The Advisory Council composed of the chairmen of the

District Business Conduct Committees (DBCC), advises the Board on matters of interest to the NASD. The Council recently recommended the following:

— Grant the DBCC and Market Surveillance Committee greater flexibility in determining whether to impose censure as a sanction in disciplinary proceedings.

— Amend the NASD By-Laws to permit filing unforeseen vacancies

on the District Nominating Committee by appointment and majority vote of the DBCC.

— Expedite the processing of fingerprints and other registration information as newly hired personnel so that members don't invest a great deal in training someone who is not employable due to an offense identified by the fingerprint check.

— Establish better lines of communication with state insurance com-

missioners regarding improper activity by insurance agents who are also registered with NASD member firms.

— Explore with the North American Securities Administrators Association (NASAA) the feasibility of developing a facility to provide members with information on registration requirements in the states.

NASD DISCIPLINARY ACTIONS

Disciplinary Actions Reported for February

The NASD® is taking disciplinary actions against the following firms and individuals for violations of the NASD Rules of Fair Practice; securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board. Unless otherwise indicated, suspensions will begin with the opening of business on Tuesday, February 16, 1993. The information relating to matters contained in this Notice is current as of the fifth of this month. Information received subsequent to the fifth is not reflected in this publication.

Firms Expelled, Individuals Sanctioned

Dillon Securities, Inc. (Spokane, Washington) and Conrad C. Lysiak (Registered Principal, Spokane, Washington). The firm was expelled from NASD membership and Lysiak was fined \$15,000 and suspended from association with any NASD member in any principal capacity for 10 days. In addition, Lysiak must requalify by examination as a general securities principal. The National Business Conduct Committee (NBCC) imposed the sanctions on Lysiak following an appeal of a District 3 District Business Conduct Committee (DBCC) decision.

The sanctions were based on findings that the firm participated in the illegal distribution of unregistered securities. In addition, a private company compensated the firm in exchange for becoming the first market maker in the company's stock. Furthermore, the firm submitted an application to the National Quotations Bureau containing false and intentionally misleading information.

Also, the firm and Lysiak failed to establish, implement, and enforce

reasonable supervisory measures necessary to prevent and detect the violations for which they were sanctioned, and to otherwise supervise certain employees' conduct.

Lysiak has appealed this action to the Securities and Exchange Commission (SEC), and his sanctions are not in effect pending consideration of the appeal.

MLB Investments, Ltd. (Denver, Colorado), Fred A. Borries, Jr. (Registered Principal, Lakewood, Colorado), James W. Magner (Registered Representative, Denver, Colorado), Charles W. Day, Jr. (Registered Principal, Denver, Colorado), and Kenneth L. Lucas (Registered Principal, Englewood, Colorado). The firm was fined \$50,000, expelled from membership in the NASD, and required to pay \$132,928 in restitution to public customers. Borries was fined \$10,000, suspended from association with any NASD member in any capacity for 30 days, suspended from association with any NASD member in any principal capacity for one year, and required to requalify by examination as a general securities principal. Magner was fined \$10,000 and suspended from association with any NASD member in any capacity for three months, and Day was barred from association with any NASD member in any capacity.

Lucas submitted an Offer of Settlement pursuant to which he was suspended from association with any NASD member in any capacity for 30 days, suspended from association with any NASD member in any principal capacity for one year, and required to requalify by examination as a principal. The sanctions were based on findings that, in violation of the NASD's Mark-Up Policy, the firm, acting through Magner, Borries and

Day, effected transactions in a common stock at prices that were not reasonably related to the prevailing market price with markups ranging from 45 to 130 percent over the prevailing market price. Moreover, the findings stated that, in furtherance of the scheme, these respondents engaged in and induced others to engage in deceptive and fraudulent devices and contrivances in transactions in the stock. The firm, acting through Day, engaged in a distribution of the same common stock while no registration statement regarding such securities was in effect with the SEC.

The firm, acting through Day, also solicited its customers to purchase the same stock and executed purchases and sales of the stock for its own account while it was engaged in a distribution of the stock. Furthermore, the firm, acting through Day, manipulated the market price for the stock by effecting a series of transactions with the intention and effect of creating actual and apparent trading activity in the same stock and raising and maintaining the price of the stock. The activity induced the purchase and sale of the stock by others. Without admitting or denying the allegations, Lucas consented to the described sanctions and to the entry of findings that Borries and Lucas failed to properly supervise the activities of the firm's associated persons.

Lucas' suspension commenced with the opening of business December 21, 1992.

Firms Suspended, Individuals Sanctioned

First Choice Securities Corporation (Englewood, Colorado), Sheldon O. Fertman (Registered Principal, Denver,

Colorado), and Gregory F. Walsh (Registered Principal, Los Angeles, California). The firm was fined \$100,915.62, jointly and severally with Fertman and fined \$50,000, separately. In addition, the firm was suspended from all principal transactions for 30 days. Fertman was fined \$50,000, separately, and barred from association with any NASD member in any capacity. The NASD fined Walsh \$63,261.87 and ordered him to requalify by examination before acting in any capacity.

The sanctions were based on findings that the firm, acting through Fertman, effected principal sales or caused customer orders to be received and processed for purchases of securities at unfair and unreasonable prices. The markups on these trades ranged from 5.44 to 60 percent over the firm's contemporaneous cost for the securities, in violation of the NASD's Mark-Up Policy.

Furthermore, the firm and Fertman failed to disclose to customers that they were charged unfair and unreasonable prices.

Also, Walsh either solicited the customers to purchase the aforementioned stock, or otherwise caused customer orders to be received and processed for purchases of these securities at unfair and unreasonable prices. In addition, Walsh failed to disclose the excessive markups to his customers.

Southeastern Capital Group, Inc. (Maitland, Florida) and Richard Tobitt Wagner (Registered Principal, Maitland, Florida). The firm was fined \$25,000 and suspended from NASD membership for 90 days. Wagner was fined \$25,000 and barred from association with any NASD member in a supervisory or principal capacity.

The sanctions were based on findings that the firm, acting through Wagner, conducted a securities business while failing to maintain its required minimum net capital and filed materially inaccurate FOCUS Part I and IIA reports. Also, the firm, acting through Wagner, failed to maintain accurate books and records and to file its annual audited financial report in a timely manner.

York Securities, Inc. (New York, New York) and David J. Corcoran (Registered Principal, Manhasset, New York) submitted an Offer of Settlement pursuant to which they were fined \$10,000, jointly and severally and each was suspended from conducting certain block trading activity.

Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that they engaged in an unregistered distribution of common stock and warrants of a blind pool. Specifically, the NASD found that York and Corcoran sold the stock and warrants and consequently acted as underwriters for the distribution. According to the findings, the respondents engaged in this activity when they knew, or should have known, that no registration statement had been filed with the SEC, and that no exemption from registration for such transactions was available.

Firms Fined, Individuals Sanctioned

B. C. Christopher Securities Company (Kansas City, Missouri) and Richard Coe Garton (Registered Representative, Kansas City, Kansas). The firm was fined \$50,000, and Garton was fined

\$30,000 and suspended from association with any NASD member in any capacity for six months. The NBCC imposed the sanctions following an appeal of a District 4 DBCC decision. The sanctions were based on findings that the firm, acting through Garton, failed to maintain accurate supervisory procedures and to properly supervise a sales representative of the firm. In addition, the firm, acting through Garton, permitted the same individual to function as a general securities representative without proper registration with the NASD.

Gateway Securities, Inc. (Greenwich, Connecticut), Holmer P. Gronager (Registered Principal, Amelia Island, Florida), and David E. Weston (Registered Representative, Miami Beach, Florida). The firm and Gronager were fined \$25,000, jointly and severally, and Gronager was barred from association with any NASD member in any capacity. Weston was fined \$25,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 11 DBCC decision. The sanctions were based on findings that the firm, Gronager, and Weston failed to pay a \$227,250 arbitration award.

Lake Securities, Inc. (Lewisville, Texas) and Huey B. Hicks (Registered Principal, Lewisville, Texas) were fined \$15,000, jointly and severally, and Hicks was required to requalify by examination as a general securities principal. The SEC imposed the sanctions following an appeal of an August 1990 NBCC decision. The sanctions were based on findings that the firm, acting through Hicks, purchased exempt securities with a face amount of \$4 million from an institutional customer and charged a

price that included an excessive markdown of 7.4 percent, which generated more than \$90,000 in profit.

Firms and Individuals Fined

AIBC Investment Services Corp. (Miami, Florida), William Burdette (Registered Principal, Coral Gables, Florida), and Wifredo Gort (Registered Principal, Miami, Florida) submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were fined \$12,500, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanction and the entry of findings that the firm, acting through Burdette and Gort, conducted a securities business while failing to maintain its required minimum net capital. In addition, the NASD found that the firm, acting through Burdette and Gort, operated without a registered financial and operations principal, in violation of Schedule C of the NASD's By-Laws.

Simmons and Bishop Co., Inc. (Scottsdale, Arizona) and Evelyn K. Simmons (Registered Principal, Scottsdale, Arizona) submitted an Offer of Settlement pursuant to which they were fined \$10,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that they failed to supervise the activities of two registered representatives adequately. Specifically, as a result, these registered representatives improperly used customer funds and another representative opened accounts at the firm before he was effectively registered with the firm.

Thomas F. White & Co., Inc. (San Francisco, California), John Warren Boudinot (Registered Representative, San Francisco, California), and Henry Walter Bineault (Registered Principal, Danielson, Connecticut) were fined \$10,000, jointly and severally. In addition, the firm was ordered to refund \$19,509 to the purchasers of securities for markups that exceeded 5 percent.

The NBCC imposed the sanctions following appeal of a District 1 DBCC decision. The sanctions were based on findings that the firm, acting through Boudinot and Bineault, failed to comply with the NASD's Mark-Up Policy in that it effected 34 corporate securities transactions as principal at unfair and unreasonable prices. The markups on these transactions ranged from 7.03 to 14.7 percent over the firm's contemporaneous cost.

Thomas F. White & Co. and Boudinot have appealed this action to the SEC, and the sanctions are not in effect pending consideration of the appeal.

Individuals Barred or Suspended

Anthony J. Amaradio (Registered Representative, Bloomfield Hills, Michigan) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000, suspended from association with any NASD member firm in any capacity for 10 business days, and required to requalify by examination as a general securities representative.

Without admitting or denying the allegations, Amaradio consented to the described sanctions and to the entry of findings that he participated in private securities transactions

with public customers without having given prior written notice to his member firm.

Angelisse Kay Athan (Registered Representative, Oldsmar, Florida) was fined \$50,000, barred from association with any NASD member in any capacity, and required to pay \$39,000 in restitution to a public customer. The sanctions were based on findings that Athan converted or misused customer funds totaling \$40,000. In addition, Athan failed to respond to an NASD request for information.

Diann J. Bright (Registered Representative, Country Club Hills, Illinois) submitted an Offer of Settlement pursuant to which she was fined \$25,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Bright consented to the described sanctions and to the entry of findings that she received from insurance customers \$315.95 in cash with instructions to use the funds as payment for insurance policies. The NASD found that Bright failed to follow the customers' instructions and used the funds for purposes other than the benefit of the customers.

The findings also stated that Bright failed to respond to NASD requests for information.

Daunice M. Bunn (Registered Representative, Johnstown, Pennsylvania) submitted an Offer of Settlement pursuant to which she was fined \$25,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Bunn consented to the described sanctions and to the entry of findings that she received cash payments for insurance premiums

totaling \$4,803.46 and failed to remit the funds to her member firm.

Joseph Dennis Catten (Registered Principal, Magna, Utah) submitted an Offer of Settlement pursuant to which he was fined \$2,500, jointly and severally with a member firm, and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Catten consented to the described sanctions and to the entry of findings that a member firm, acting through Catten, failed to prepare and maintain adequate written supervisory procedures for the types of business in which it engages.

Wayne Allen Deloney (Registered Representative, San Clemente, California) was fined \$15,780.60 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions after review of a District 2 DBCC decision. The sanctions were based on findings that Deloney accepted from insurance customers a \$604.35 check and \$176.25 in cash for the purchase of an insurance policy. Deloney cashed the check but failed to purchase the policy for the customers and converted the funds totaling \$780.60 to his personal use and benefit.

Carolyn R. Delorraine (Registered Representative, Boulder, Colorado) was fined \$11,281, suspended from association with any NASD member in any capacity for five business days, and required to requalify by examination before acting in any capacity. The NBCC imposed the sanctions on review of a District 13 DBCC decision. The sanctions were based on findings that Delorraine sold stock in the joint account of public customers without their authorization.

Also, to circumvent the requirements of SEC Rule 15c2-6, Delorraine instructed a customer to sign an inaccurate document stating that his purchase of stock was unsolicited, when in fact, Delorraine solicited the customer to purchase the stock.

Christi Ann Edwards (Registered Representative, Nashville, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which she was fined \$1,000. In addition, she completed a two-week suspension from association with any NASD member in any capacity. Without admitting or denying the allegations, Edwards consented to the described sanctions and to the entry of findings that she signed the names of two public customers to two separate subscription agreements.

George H. Ellis, IV (Registered Representative, Cary, North Carolina) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$25,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Ellis consented to the described sanctions and to the entry of findings that he effected 34 securities transactions in the accounts of seven public customers without their knowledge or authorization.

Sheldon O. Fertman (Registered Principal, Denver, Colorado) and **John J. Cox (Associated Person, Denver, Colorado)** submitted an Offer of Settlement pursuant to which Fertman was fined \$100,000 and barred from association with any NASD member in any capacity. Cox was fined \$25,000, suspended from association with any NASD member in any capacity for six months, and required to requalify

by examination as a general securities principal.

Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that, a former member firm, acting through Fertman, conducted a securities business while failing to maintain its minimum required net capital and filed an inaccurate FOCUS Part I report. The findings also stated that, in violation of SEC Rule 15c2-6, the firm, acting through Fertman, effected transactions in designated securities in 10 public customer accounts without obtaining required suitability statements before approving their accounts. The NASD also determined that the firm, acting through Fertman, failed to respond to NASD requests for information, falsified order tickets, and filed an inaccurate Form BD.

In addition, the NASD determined that the firm, acting through Fertman and Cox, allowed Cox, an unregistered person, to act as a principal of the firm and failed to disclose on the firm's Form BD that Cox was a control person with the firm. Moreover, the firm, acting through Fertman and Cox, failed to make a bona fide "minimum-maximum" contingent offering of limited partnership interests.

Furthermore, the findings stated that the firm, acting through Fertman and Cox, violated SEC Rules 10b-5 and 10b-6 by trading securities while participating as an underwriter in the stock's distribution during its initial public offering. During the distribution, the firm, Fertman, and Cox induced customers to purchase these securities at excessive prices while failing to disclose that they were purchasing the securities at excessive prices compared to the prices in the initial

public offering, according to the findings.

The NASD also determined that the firm, acting through Fertman and Cox, failed to establish, maintain, and enforce written supervisory procedures.

Dennis W. Gaddy (Registered Representative, Raleigh, North Carolina) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$20,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Gaddy consented to the described sanctions and to the entry of findings that he received a \$5,000 check from a public customer to purchase shares of a mutual fund and, instead, Gaddy negotiated the check and converted the proceeds to his own use and benefit.

Richard E. Garcia (Registered Representative, Boca Raton, Florida) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$13,200 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Garcia consented to the described sanctions and to the entry of findings that he sold securities to public customers outside the scope of his association with his member firms and without the written authorization of those firms. The findings also stated that, in the above transactions, Garcia received \$32,000 from the customers to buy securities and processed those funds through the bank account of a corporation he owned before he forwarded the funds to the issuer.

In addition, the NASD found that Garcia sent a letter to public customers on the stationery of his

member firm without prior approval of the letter by a principal. Also, according to the findings, Garcia provided a public customer with a letter guaranteeing the customer against loss on an investment.

Gordon T. Gould (Registered Principal, Washington, D.C.) was fined \$10,000 and barred from association with any NASD member as a financial and operations principal. The NBCC imposed the sanctions following an appeal of a District 9 DBCC decision. The sanctions were based on findings that a former member firm, acting through Gould, provided investors with an offering memorandum that failed to disclose certain material information.

In addition, the firm, acting through Gould, filed FOCUS Parts I and IIA reports with inaccurate net capital computations and filed a late annual audited report. Gould, acting for the firm, also conducted a securities business without its minimum required net capital. Furthermore, Gould failed to provide telegraphic notice of material inadequacies in the firm's internal controls.

Michael George Gundzik (Registered Representative, Greenwood Village, Colorado) submitted an Offer of Settlement pursuant to which he was fined \$20,000 and suspended from association with any NASD member in any capacity for 180 days. Without admitting or denying the allegations, Gundzik consented to the described sanctions and to the entry of findings that he collected from two insurance customers premiums for disability insurance totaling \$2,360.22. According to the findings, Gundzik deposited the funds into his business account thereby commingling the monies with other funds. The NASD determined that Gundzik, thereafter, sent checks to

his member firm to pay for those policies, but the bank returned the checks for insufficient funds.

Tran Du Hong (Registered Representative, Orange, California) submitted an Offer of Settlement pursuant to which he was fined \$23,602.30 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Hong consented to the described sanctions, and to the entry of findings that he accepted from 13 insurance customers cash or checks totaling \$3,628.30 intended for the payment of premiums and converted the funds to his own use.

Robert Harry Joyce (Registered Principal, Arvada, Colorado) submitted an Offer of Settlement pursuant to which he was suspended from association with any NASD member in any capacity for 15 business days. Without admitting or denying the allegations, Joyce consented to the described sanction and to the entry of findings that he failed to execute sell orders for four customers and supplied three of those customers with false and misleading quotations.

The findings also stated that Joyce made price projections to a customer without having a reasonable basis for these projections and offered to reimburse another customer against loss.

Roland K. Kaeser (Registered Principal, Barrington Hills, Illinois) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 30 days. In addition, he must requalify by examination as a general securities representative.

Without admitting or denying the allegations, Kaeser consented to the described sanctions and to the entry of findings that he participated in private securities transactions and outside business activities while failing to notify his member firm.

Gary K. Kertzman (Registered Representative, Deerfield Beach, Florida) was fined \$50,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Kertzman effected a series of transactions for the joint securities account of two public customers without their knowledge or authorization. To avoid detection of the unauthorized transactions, Kertzman changed the account address to his personal address. In addition, Kertzman failed to respond to an NASD request for information.

Paul C. Kettler (Registered Principal, Chicago, Illinois) was fined \$10,000 and suspended from association with any NASD member in any capacity for 30 days. In addition, he must requalify by examination as a general securities principal. The SEC imposed the sanctions following an appeal of a June 1991 NBCC decision. The sanctions were based on findings that a former member firm, acting through Kettler, employed an individual and permitted him to be associated with the firm when Kettler knew or should have known that the individual was barred from such employment or association by the NASD.

Kenneth L. Koch (Registered Representative, Pinconning, Michigan) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$1,000 and barred from association with any NASD member in any capacity. Without admitting or

denying the allegations, Koch consented to the described sanctions and to the entry of findings that he received from insurance customers \$165 in cash with instructions to use such funds to make an automobile insurance payment. The NASD found that Koch failed to follow the customers' instructions and used the funds for his personal benefit.

Richard L. Larew (Registered Principal, Ft. Lauderdale, Florida) was fined \$25,000, suspended from association with any NASD member in any capacity for 15 business days, and required to pay \$4,386.09 in restitution to public customers. The sanctions were based on findings that Larew purchased common stocks for the accounts of public customers without their knowledge or authorization.

James H. Mara (Registered Representative, Michigan City, Indiana) submitted an Offer of Settlement pursuant to which he was fined \$25,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Mara consented to the described sanctions and to the entry of findings that he received from an insurance customer \$4,859.69 in cash with instructions to pay for life insurance policies. The NASD determined that Mara applied \$1,020.30 to the payment and used the balance of \$3,839.39 for his personal benefit.

Eddie L. McNeill (Registered Representative, Pasadena, Texas) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$50,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, McNeill consented to the described sanctions and to the

entry of findings that he received from two public customers \$42,246.12 to invest in corporate bonds and money market funds but failed to submit the monies to his member firm. Instead, the findings stated that McNeill converted the funds to his own use without the customers' knowledge or consent.

The NASD also found that McNeill used those funds to buy certificates of deposit through a non-registered brokerage entity and sent fraudulent confirmations and account statements to his two customers. In addition, the NASD determined that McNeill failed to provide his member firm with written notice of his affiliation with an outside business activity.

Robert David Meerkreebs (Registered Representative, La Jolla, California) was fined \$25,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 2 DBCC decision. The sanctions were based on findings that Meerkreebs participated in private securities transactions while failing to provide prior written notification to his member firm.

William Hilton Money, Jr. (Registered Representative, Ventnor, New Jersey) submitted an Offer of Settlement pursuant to which he was suspended from association with any NASD member in any capacity for three business days. Without admitting or denying the allegations, Money consented to the described sanctions and to the entry of findings that he failed to pay a \$3,820.80 arbitration award in full.

Robert Wright Morgan (Registered Representative, Casselberry, Florida) submitted an Offer of Settlement pursuant to

which he was fined \$30,000, barred from association with any NASD member in any capacity, and required to pay restitution to public customers.

Without admitting or denying the allegations, Morgan consented to the described sanctions and to the entry of findings that he received from two public customers \$73,351.63 with instructions to purchase shares of common stocks. Instead, the findings stated that Morgan purchased only \$58,579.13 worth of the stocks, misused the remaining \$14,772.50, and failed to return the balance to the customers. The NASD also found that Morgan issued a series of fictitious client statements to these customers and misused their securities. In addition, the NASD determined that Morgan guaranteed the same customers against loss when buying common stocks.

Furthermore, the findings stated that Morgan opened a securities account at a member firm and failed to inform the firm that he was associated with another member firm. Also, according to the findings, Morgan participated in private securities transactions without providing his member firm with prior written notice. The findings also stated that Morgan executed the aforementioned securities transactions without being properly registered.

William Louis Morgan (Registered Principal, Danville, California) was barred from association with any NASD member in any capacity. The NBCC imposed the sanction following appeal of a District 1 DBCC decision. The sanction was based on findings that Morgan participated in private securities transactions without providing prior written notification to his member firm.

This action has been appealed to the SEC, and the sanctions, other than the bar, are not in effect pending consideration of the appeal.

Donald Harvey Norris (Registered Representative, Orange Park, Florida) was barred from association with any NASD member in any capacity. The sanction was based on findings that Norris solicited and received checks from public customers totaling \$176,816.66 for investment purposes and, instead, converted the funds to his own use and benefit without the customers' knowledge or consent. In addition, Norris failed to respond to NASD requests for information.

Roger Lee Parsons (Registered Principal, Baltimore, Ohio) submitted an Offer of Settlement pursuant to which he was fined \$165,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Parsons consented to the described sanctions and to the entry of findings that a former member firm, acting through Parsons, effected securities transactions while failing to maintain its required minimum net capital and failed to report its non-Nasdaq securities volume. The NASD also found that the firm, acting through Parsons, failed to prepare and maintain completed suitability statements and written agreements before the initial purchase of securities, in violation of SEC Rule 15c2-6.

In addition, the NASD determined that the same firm, acting through Parsons, effected transactions in a common stock at unfair and unreasonable prices, causing \$85,474 in excess markups. These markups ranged from 11.11 to 90.48 percent, in violation of NASD's Mark-Up Policy. Also, according to the find-

ings, Parsons failed to maintain adequate written supervisory procedures designed to assure compliance with SEC Rule 15c2-6 and failed to supervise an employee of his member firm.

Anne T. Peters (Registered Representative, Scranton, Pennsylvania) was fined \$23,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Peters received from an insurance customer \$242.50 in cash as payment for a life insurance premium. Peters failed to submit the money with the application and subsequently submitted personal checks that were not honored when presented for payment due to insufficient funds. Peters also failed to respond to NASD requests for information.

Anthony Lee Rick (Registered Representative, Boca Raton, Florida) submitted an Offer of Settlement pursuant to which he was fined \$5,000, suspended from association with any NASD member in any capacity for six months, and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Rick consented to the described sanctions and to the entry of findings that he converted customer funds totaling \$1,000 to his own use and benefit. In addition, Rick failed to respond to an NASD request for information.

Michael S. Rohdenburg (Registered Representative, Elmhurst, Illinois) was fined \$30,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Rohdenburg filed with two member firms new account cards containing false and inaccurate information regarding a

customer. Also, in contravention of the Board of Governors' Free-Riding and Withholding Interpretation, Rohdenburg sold shares of a "hot issue" to a restricted person.

In addition, Rohdenburg transferred customer accounts from one member firm to another without the customers' knowledge or consent.

Rodney Alan Ruzanic (Registered Representative, Palm Harbor, Florida) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that, as principal for his own account, Ruzanic effected private securities transactions with public customers at an unfair price. Furthermore, he failed to provide prior written notice to his member firm of his intent to engage in these private transactions. In addition, Ruzanic failed to respond to an NASD request for information.

Kevin J. Sakser (Registered Principal, Marietta, Georgia) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$20,000 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Sakser consented to the described sanctions and to the entry of findings that he effected eight unauthorized securities transactions in the account of a public customer. The NASD also found that Sakser changed the account address to a fictitious one.

Kevin Michael Short (Registered Principal, Encino, California) was fined \$10,000 and barred from association with any member of the NASD in any capacity. The sanctions were based on findings that

Short failed to respond to NASD requests for information.

Roy Smith (Registered Principal, Jacksonville, Florida) was fined \$5,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Smith failed to pay a \$1,611 arbitration award.

Thomas Sparks (Registered Representative, Scottsdale, Arizona) submitted an Offer of Settlement pursuant to which he was fined \$1,000, suspended from association with any NASD member in any capacity for 90 days, and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Sparks consented to the described sanctions and to the entry of findings that, while taking a qualification examination, he had in his possession unauthorized material in the testing center.

Brian Robert Subatich (Associated Person, Chicago, Illinois) submitted an Offer of Settlement pursuant to which he was fined \$1,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Subatich consented to the described sanctions and to the entry of findings that he submitted to his member firm a false Series 6 examination score sheet.

Lorin W. Surpless (Registered Representative, Tucson, Arizona) submitted an Offer of Settlement pursuant to which he was suspended from association with any NASD member in any capacity for nine months and required to requalify by examination before acting in any capacity. Without admitting or denying the allegations, Surpless consented to the described sanc-

tions and to the entry of findings that he solicited customers to buy securities by misrepresenting, and failing to disclose, material facts to them. These misrepresentations included statements regarding the proposed performance and lack of risk of the investment.

The NASD also determined that Surpluss recommended the purchase of the aforementioned securities to customers without having reasonable grounds for believing that such recommendations were suitable for the customers.

J. Speed Thomas (Registered Principal, Nashville, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$2,500. In addition, he has completed an eight-week suspension from association with any NASD member in any capacity. Without admitting or denying the allegations, Thomas consented to the described sanctions and to the entry of findings that he signed the names of five public customers to five separate subscription agreements.

David C. Thompson (Registered Representative, Muncy, Pennsylvania) submitted an Offer of Settlement pursuant to which he was fined \$5,000 and barred from association with any member of the NASD in any capacity. Without admitting or denying the allegations, Thompson consented to the described sanctions and to the entry of findings that he received cash payments totaling \$164.68 for insurance premiums which he failed to remit timely to his member firm. The NASD also found that Thompson failed to respond to NASD requests for information.

Philip J. Tomko (Registered Representative, Bloomsburg, Pennsylvania) was fined \$25,000

and barred from association with any NASD member in any capacity. The sanctions were based on findings that Tomko induced a public customer to issue a \$3,000 check to him to purchase stock for her. Thereafter, Tomko cashed the check for his own use and benefit.

Peter J. Uttley (Registered Representative, Berkeley, California) submitted an Offer of Settlement pursuant to which he was fined \$75,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Uttley consented to the described sanctions and to the entry of findings that he obtained from a public customer \$43,000 with instructions to use the funds for various investments. The NASD found that Uttley failed to follow the customer's instructions and retained the funds for his personal use and benefit.

The findings also stated that Uttley failed to respond to NASD requests for information.

Dean E. Walker (Registered Representative, Kezar Falls, Maine) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for five business days. Without admitting or denying the allegations, Walker consented to the described sanctions and to the entry of findings that he issued bad personal checks to his member firm totaling \$59,789 to pay for transactions in his securities accounts. In addition, the NASD found that Walker executed unauthorized transactions in the account of two public customers.

Wayne D. Wheeler (Registered Representative, Florida, New York) was fined \$10,000 and

barred from association with any NASD member in any capacity. The sanctions were based on findings that Wheeler failed to respond to NASD requests for information concerning a customer complaint.

Scott Allan Wilcox (Registered Representative, Plantation, Florida) was fined \$47,965 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Wilcox converted customer funds totaling \$2,965 to his own use and benefit without the customer's knowledge or authorization. In addition, Wilcox failed to respond to an NASD request for information.

Bruce Martin Zipper (Registered Principal, Miami, Florida) was fined \$5,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 7 DBCC decision. The sanctions were based on findings that Zipper failed to pay a \$418,000 arbitration award.

Zipper has appealed this action to the SEC, and the sanctions are not presently in effect pending consideration of a temporary interim stay pending review of stay request and the merits of the appeal.

Individuals Fined

Lyle Reinhard Haas (Registered Principal, Veradale, Washington) was fined \$15,000, jointly and severally with a former member firm and required to requalify by examination as a financial and operations principal. The NBCC imposed the sanctions following an appeal of District 3 DBCC decision. The sanctions were based on findings that the firm, acting through Haas, conducted a securities business

while failing to maintain its minimum required net capital.

Firms Expelled for Failure to Pay Fines and Costs in Connection With Violations

Lake Securities, Incorporated,
Lewisville, Texas

Firms Suspended

The following firms were suspended from membership in the NASD for failure to comply with formal written requests to submit financial information to the NASD. The actions were based on the provisions of Article IV, Section 5 of the NASD Rules of Fair Practice and Article VII, Section 2 of the NASD By-Laws. The date the suspension commenced is listed after each entry. If the firm has complied with the requests for information, the listing also includes the date the suspension concluded.

Boston International Group Securities Corp., Boston,
Massachusetts (January 11, 1993)

Lone Star Securities, Inc.,
Abilene, Texas (January 11, 1993)

Individual Barred for Failure to Comply With Sanctions Imposed

Larry L. Franke, Englewood,
Colorado

Individuals Whose Registrations Were Revoked for Failure to Pay Fines and Costs in Connection With Violations

Howard Alweil, Sherman Oaks,
California

Richard M. Bettencourt, Matawan,
New Jersey

Steven A. Braker, Backus,
Minnesota

Stephen E. Cayou, Lakewood,
Colorado

Sheldon O. Fertman, Denver,
Colorado

Huey B. Hicks, Lewisville, Texas

Stewart E. Holzkenner, New York,
New York

Stuart L. Huber, Huntington, New
York

Duane K. Musgrove, Brooklyn
Park, Minnesota

Jack W. Pruitte, Clarksville,
Tennessee

Jeffrey R. Skinner, Littleton,
Colorado

Richard L. Sumrall, Glendale,
Colorado

Richard R. Whatley, Rancho Palos
Verdes, California

NASD Announces Disciplinary Actions Against National Securities Corporation and Nine Individuals

The NASD has announced a disciplinary action taken by the Market Surveillance Committee (MSC) against National Securities Corporation (NATL), William Sheppard, Jeffrey J. Pritchard, Lynette M. LaRue, Robert F. Nagel, Andrew C. Berry, Bruce E. Mauer, Mark A. Anderson, Brian P. Gentry, and Richard L. Blackstock. Except for Sheppard, the NASD accepted offers of settlement from all respondents, who consented to findings by

the MSC of facts and violations consistent with the allegations in the Complaint without admitting or denying those allegations.

Because he failed to file an answer or appear at the hearing, the NASD barred Sheppard from association with any member of the NASD in any capacity and fined him \$500,000.

Pursuant to the acceptance of the offers of settlement submitted by the remaining respondents, NATL was fined \$80,000 and agreed to a number of undertakings, most of which involve significant supervision and compliance initiatives; Pritchard was fined \$10,000 and suspended in all capacities from association with any NASD member for 120 days; LaRue was fined \$150,000 and suspended in all capacities from association with any member for five years; Nagel was fined \$5,000 and suspended in all capacities from association with any member for three years; Berry was fined \$20,000 and suspended in all capacities from association with any member for 30 days; Mauer was suspended in all capacities from association with any member for two years; Anderson was fined \$12,000 and barred in all capacities from association with any member; Gentry was fined \$25,000 and suspended in all capacities from association with any member for two years; and Blackstock was suspended in all capacities from association with any member for 21 days.

The NASD alleged that from on or about March 1990 through June 1990, Sheppard, LaRue, Nagel, Mauer, and Berry, by and through, Delta & Parker, Inc. (D&P). D&P (a corporation in which these individuals were the sole shareholders which owned the Englewood, Colorado franchise branch office of National Securities Corporation,

violated Sections 1 and 18 of the NASD Rules of Fair Practice, Section 10(b) of the Securities Exchange Act of 1934 (Exchange Act) and Rule 10b-5 thereunder. Section 18 and Rule 10b-5 prohibit the use of any manipulative, deceptive, or other fraudulent device in the purchase or sale of any security. The Complaint alleged that the respondents engaged in a manipulative, fraudulent, and deceptive scheme which included, among other things, purchasing the common stock of Vintage Group, Inc. (VINT) using funds attained from resales of VINT to retail customers, and engaging in abusive, fraudulent, and high-pressure sales practices designed to increase the demand, and thus, the price of the security. Moreover, the Complaint alleges that these respondents arranged transactions in violation of Regulation T and X of the Federal Reserve Board. The Complaint also alleged that Sheppard, LaRue, Nagel, Mauer, Berry, Anderson, Gentry, and Blackstock effected unauthorized transactions, made unsuitable recommendations, exercised discretion in accounts without

written authority, provided guarantees against loss, failed to follow customer instructions, or made misrepresentations to customers in the sale of VINT common stock. The Complaint further alleged that Sheppard violated Sections 1 and 28 of the NASD Rules of Fair Practice by failing to conduct transactions for or by persons associated with NASD members in accordance with the provisions of those rules. Finally, the Complaint alleges that NATL and Pritchard failed to supervise to prevent the above alleged violations of Sections 1 and 27 of the NASD Rules of Fair Practice.

The NASD also filed a separate Complaint action relating solely to Gentry's failure to provide information requested by the NASD's Market Surveillance Department in its investigation into trading in the securities of VINT. Among other things, Gentry failed to appear for on-the-record testimony, although subsequent to the filing of the Complaint, he did appear before the staff. He also submitted an offer of settlement to this separate Complaint action, and the sanctions

imposed reflect the violative conduct alleged in both Complaints.

The investigation leading to this action was conducted by the NASD's Market Surveillance Department which utilizes sophisticated technology in monitoring activity in The Nasdaq Stock MarketSM and other markets operated or regulated by the NASD.

The MSC, which consists of 12 professionals from securities firms across the country, is charged with the responsibility for disciplining NASD members and their associated persons who fail to comply with market-related rules and securities laws.

The suspensions for Pritchard, LaRue, Nagel, Berry, Gentry, and Blackstock commenced January 18, 1993. Respondent Mauer is currently suspended until October 19, 1994, as a result of a previous MSC disciplinary action, and therefore the suspension in this case will begin October 20, 1994.

NASD NOTICE TO MEMBERS 93-15

Mail Vote — Proposed Amendments to Articles VII and XII of the NASD By-Laws and Article III of The NASD Rules of Fair Practice to Make All Rule Approval Procedures Under the By-Laws Uniform; **Last Voting Date: April 23, 1993**

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD invites members to vote on a proposed amendment to the NASD By-Laws and Rules of Fair Practice to make all rule approval procedures under the NASD's By-Laws uniform (presently some need only Board approval; others need full membership approval) and to convert Appendices into Rules of Fair Practice. The last voting date is April 23, 1993. The text of the amendment follows this Notice.

Background and Description of Proposal

The proposed amendments are the first of a multi-part program, the purpose of which is to make all rule approval and amendment procedures under the NASD's By-Laws uniform and to make the *NASD Manual* easier to use. Presently some Rules of Fair Practice need only Board approval for amendment; others need full membership approval.

Below are the changes to the By-Laws needed to make the voting procedures uniform. The proposal removes the member-vote requirement for adoption of or amendments to the Rules of Fair Practice and other rules. This action would make the NASD's procedures consistent with those of other self-regulatory organizations in the securities industry, which do not require member votes for rule changes. The proposal would not only reduce delays in making rule changes effective, but would also result in administrative cost savings. Amendments to the NASD's By-Laws would continue to require a member vote, and the Board has specifically provided in the proposed amendments that it may seek a member vote on any rule change if it feels such a vote is desirable.

Section 1(a)(1) of Article VII of the By-Laws has been divided into two subsections, since amendments to the By-Laws would continue to require a member vote. New subsection (2) would specify that the Board has the authority to adopt or to change the Rules of Fair Practice, and that it can still choose to submit certain rule changes to the membership for a vote at its option.

Amendments to Article VII, Sections 1(a)(3), (4), and (6) of the By-Laws would remove superfluous language therein specifying that no member vote is needed. The deleted provisions are in brackets. New Section 1(a)(2) states that the Board has authority to adopt Rules of Fair Practice. Amended Section 1(a)(3) gives a broader grant of authority to the Board to adopt such rules as are necessary to "implement the provisions of the Act."

Existing subsection (9) is proposed to become new subsection (3) with language in that subsection specifically referencing the Government Securities Act of 1986 deleted because the pertinent provisions of that Act are part of the Securities Exchange Act of 1934, as amended (the Act). The amended subsection contains general authorization to the Board to adopt rules to implement the provisions of the Act.

Article XII, Section 1 of the By-Laws is also proposed to be amended to delete the reference to the member vote procedure for adoption and amendment of Rules of Fair Practice, and to remove references to emergency rules.

Certain of the Rules of Fair Practice themselves specify that a member vote is not required as to rules in a specified category and that the Board itself can adopt these rules. Because of the By-Laws changes,

this language will no longer be necessary. Shown below are proposed amendments to those rules, which will eliminate the unnecessary language.

Article III, Sections 30 through 34 of the Rules of Fair Practice have appendices that, as adopted, contain substantive rule provisions in the respective areas where the Board was given authority by the rules to act without a member vote. These appendices are proposed to be converted to rules and appropriate changes have, therefore, been made. Also deleted are the provisions authorizing the types of rules specified and stating how the appendices may be amended. Authorization is adequately covered in Article VII of the By-Laws, and the amendment procedure is left to the Board by that Article.

Section 37, which authorizes the ITS/CAES and CAES Operating Rules, has been deleted completely, as such authorization is contained in Article VII, new subsections 1(a)(3), (8), and (9).

Request for Vote

The NASD Board of Governors believes that the proposed amendments to the Rules of Fair Practice will aid the Board in approving and amending Rules of Fair Practice in a timely manner, subject to approval by the Securities and Exchange Commission, without the costs and delays inherent in sending proposed rule changes to nearly 6,000 members for a mail vote. Rule changes would continue to be announced to the membership, and a comment period is always provided subsequent to SEC publication of a proposed rule change in the *Federal Register*. In addition, the SEC requires the NASD to consider and respond to all comments

received from members and the public on a proposed change to NASD rules. Therefore, members will have adequate opportunity for their comments and concerns to be addressed. Please mark the attached ballot according to your convictions and mail it in the enclosed, stamped envelope to The Corporation Trust Company. Ballots must be post-marked no later than April 23, 1993.

Questions concerning this Notice should be directed to T. Grant Callery, Vice President and General Counsel, at (202) 728-8285.

Proposed Amendments to Articles VII and X of the NASD By-Laws

(Note: New text is underlined; deleted text is in brackets.)

* * * * *

Article VII

Board of Governors Powers and Authority of Board of Governors

Sec. 1. (a) The Board of Governors shall be the governing body of the Corporation and, except as otherwise provided by these By-Laws, shall be vested with all powers necessary for the management and administration of the affairs of the Corporation and the promotion of the Corporation's welfare, objects and purposes. In the exercise of such powers, the Board of Governors, shall have the authority to:

(1) adopt for submission to the membership, as hereinafter provided, such By-Laws[, Rules of Fair Practice] and changes or additions thereto as it deems necessary or appropriate;

(2) adopt such Rules of Fair

Practice and changes or additions thereto as it deems necessary or appropriate, provided, however, that the Board may at its option submit to the membership any such adoption, change, or addition to the Rules of Fair Practice;

[(9)] (3) (a) adopt [for submission to the membership] such rules as the Board of Governors deems appropriate to implement the provisions of the Act as amended [by the Government Securities Act of 1986] and the rules and regulations promulgated thereunder, and (b) make such regulations, issue such orders, resolutions, interpretations, including interpretations of the rules adopted pursuant to this Section, and directions, and make such decisions as it deems necessary or appropriate.

[(2)] (4) Unchanged.

[(3)] (5) prescribe a code of arbitration procedure providing for the required or voluntary arbitration of controversies between members and between members and customers or others as it shall deem necessary or appropriate[, and neither the adoption nor any amendments to the code need be submitted to the membership for approval and the code and any amendments thereto shall become effective as the Board of Governors may prescribe];

[(4)] (6) establish rules and procedures to be followed by members in connection with the distribution of securities issued by members and affiliates thereof[, and neither the adoption nor any amendments to such rules and procedures need be submitted to the membership for approval and such rules and procedures and any amendments thereto shall become effective as the Board of Governors may prescribe];

[5] (7) Unchanged.

[(6)] (8) organize and operate automated systems to provide qualified subscribers with securities information and automated services. The systems may be organized and operated by a division or subsidiary company of the Corporation or by one or more independent firms under contract with the Corporation as the Board of Governors may deem necessary or appropriate. The Board of Governors may adopt rules for such automated systems, establish reasonable qualifications and classifications for members and other subscribers, provide qualification standards for securities included in such systems, require members to report promptly information in connection with securities included in such systems, and establish charges to be collected from subscribers and others. [The Board of Governors shall have power to adopt, amend, supplement or modify such rules, qualifications, classifications, standards and charges from time to time without recourse to the membership for approval, and such rules, qualifications, classifications, standards and charges shall become effective as the Board of Governors may prescribe; and];

[(7)] (9) require the prompt reporting by members of such original and supplementary trade data as the Board deems appropriate. Such reporting requirement may be administered by the Corporation, a division or subsidiary thereof, or a clearing agency registered under the Securities Exchange Act of 1934[.]; and

[(8)] (10) engage in any activities or conduct necessary or appropriate to carry out the Corporation's purposes under its Certificate of Incorporation and the federal securities laws.

(b) Unchanged.

* * * * *

Article XII

Rules of Fair Practice

Sec. 1. To promote and enforce just and equitable principles of trade and business, to maintain high standards of commercial honor and integrity among members of the Corporation, to prevent fraudulent and manipulative acts and practices, to provide safeguards against unreasonable profits or unreasonable rates of commissions or other charges, to protect investors and the public interest, to collaborate with governmental and other agencies in the promotion of fair practices and the elimination of fraud, and in general to carry out the purposes of the Corporation and of the Act, the Board of Governors is hereby authorized to adopt [for submission to the members of the Corporation] such Rules of Fair Practice for the members and persons associated with members, and such amendments thereto as it may, from time to time, deem necessary or appropriate. [The Board of Governors, upon the adoption of any such Rules of Fair Practice or amendments thereto, shall forthwith cause copies thereof to be sent to each member of the Corporation to be voted upon.] If any such Rules of Fair Practice or amendments thereto [are approved by a majority of the members voting, within thirty (30) days after the date of submission to the membership, and] are approved by the Commission as provided in the Act, they shall become effective Rules of Fair Practice of the Corporation as of such date as the Board of Governors may prescribe. [In any case, however, where a particular provision of a Rule of Fair Practice provides that membership approval is

not required, the Board may amend that provision without submission to the membership for a vote as hereinbefore required. In addition, where the Board of Governors by resolution finds an emergency to exist, such Rules of Fair Practice of amendments thereto, if adopted by a two-thirds vote of the Board of Governors, may become effective as of such time as the Board of Governors may prescribe, without submission to the members for a vote as hereinbefore required. An emergency which is found by the Board of Governors to exist shall continue until the Board of Governors by resolution terminates such but in no event shall an emergency continue for a period in excess of six months. The Board of Governors shall have the authority, however, after, in each instance, reassessing the facts and circumstances which gave rise to the emergency, by resolution to declare, if it deems such appropriate under the facts and circumstances then existing, the emergency to continue to exist for successive six-month periods as required. All emergency rules adopted during the period of the emergency shall cease to be effective upon the termination of the emergency as hereinbefore provided.] The Board of Governors is hereby authorized, subject to the provisions of the By-Laws and the Act, to administer, enforce, suspend, or cancel any Rules of Fair Practice adopted hereunder.

Proposed Amendments to Article III of the NASD Rules of Fair Practice

* * * * *

Margin Accounts

Sec. 30.

[Prohibition]

[(a) A member shall not effect a securities transaction in a margin account in a manner contrary to the requirements adopted by the Board of Governors pursuant to authority granted by this rule nor shall a member in connection with such a transaction otherwise act in a manner inconsistent with requirements adopted hereunder.]

[Requirements]

[(b) The Board of Governors is authorized (1) to establish the minimum amounts of initial and maintenance margin required to be obtained by members from customers for or with whom such members effect transactions on a margin or cash basis, and (2) to establish other specific requirements or prohibitions, including record-keeping, reporting or other requirements necessary for the proper implementation of the initial and margin maintenance provisions.]

[Amount required]

[(c) The amounts of margin required, and other requirements authorized hereby, shall be set forth in Appendix A attached to and made part of this rule. The Board of Governors may from time to time alter, amend, supplement or modify the said Appendix A.]

[Special margin requirements]

[(d) Whenever the Board of Governors determines that unusual or extraordinary conditions warrant, it may prescribe special margin requirements for specific securities. The membership shall be promptly informed by notice to it of any such special margin requirements.]

[APPENDIX A]

The text of new Appendix A as approved by the SEC in February 24, 1993, (SEC Release No. 34-31918) is to be included here.

* * * * *

Securities “Failed to Receive” and “Failed to Deliver”

Sec. 31.

[The Board of Governors shall have the authority to establish rules, regulations and procedures to be followed by members in connection with domestic and foreign securities which are “failed to receive” and “failed to deliver.” The rules, regulations and procedures authorized hereby shall be incorporated into Appendix B to be attached to and made part of this rule. The Board of Governors shall have the power to alter, amend, supplement or modify the provisions of Appendix B from time to time without recourse to the membership for approval, as would otherwise be required by Article IX of the By-Laws. Appendix B shall become effective as the Board of Governors may prescribe unless disapproved by the Securities and Exchange Commission.]

[APPENDIX B]

The text of former Appendix B is to become new Section 31.

* * * * *

Fidelity Bonds

Sec. 32.

[Application]

[(a) Every member shall be required to carry a blanket fidelity

bond meeting requirements as to form, amount and type of coverage as the Board of Governors may prescribe pursuant to the authorization granted by paragraph (b) hereof.]

[Authority of Board]

[(b) The Board of Governors is hereby authorized to adopt rules, regulations and procedures for blanket fidelity bonds concerning the form, amount and type of coverage thereof. The rules, regulations and procedures authorized hereby shall be incorporated into Appendix C to be attached to and made part of this rule. The Board of Governors shall have the power to alter, amend, supplement or modify the provisions of Appendix C from time to time without recourse to the membership for approval, as would otherwise be required by Article VII of the By-Laws. All contemplated changes shall, however, be submitted to the membership for comment prior to effectiveness. Appendix C shall become effective as the Board of Governors may prescribe unless disapproved by the Securities and Exchange Commission.]

[APPENDIX C]

The text of former Appendix C is to become new Section 32.

* * * * *

Options

Sec. 33.

[(a) A member or a person associated with a member shall not effect any transaction in an option contract, including an option displayed on the NASDAQ System, except in accordance with the provisions of rules, regulations and procedures

adopted by the Board of Governors pursuant to the authorization granted in subsection (b) hereof.]

[(b) The Board of Governors is authorized, for the purpose of preventing fraudulent and manipulative acts and practices, promoting just and equitable principles of trade, providing safeguards against unreasonable profits or unreasonable rates of commission or other charges, and for the protection of investors and the public interest, to adopt rules, regulations and procedures for transactions in options relating to:]

[(1) transactions in option contracts, including options displayed on the NASDAQ System, by members for their own account or the accounts of public customers;]

[(2) the comparison - clearance and settlement of transactions in options;]

[(3) the reporting of transactions in options;]

[(4) the qualifications and standards for registered market makers in options;]

[(5) the standards for authorization of underlying securities eligible to be subject to options displayed on the NASDAQ System;]

[(6) the endorsement and guarantee of performance options; and,]

[(7) such other areas of options activity and trading as may be required to achieve the above-stated purposes.]

[(c) The rules, regulations and procedures authorized by subsection (b) hereof shall be incorporated into Appendix E to be attached to and made a part of these Rules of Fair Practice. The Board of Governors

shall have the power to adopt, alter, amend, supplement or modify the provisions of Appendix E from time to time without recourse to the membership for approval, as would otherwise be required by Article VII of the By-Laws, and Appendix E shall become effective as the Board of Governors may prescribe unless disapproved by the Securities and Exchange Commission.]

[(d)](a) For purposes of this section, the term "option" shall mean any put, call, straddle or other option or privilege, which is a "security" as defined in Section 2(1) of the Securities Act of 1933, as amended, but shall not include any tender offer, registered warrant, right, convertible security or any other option in respect to which the writer is the issuer of the security which may be purchased or sold upon the exercise of the option.

(b) [APPENDIX E]

The text of former Appendix E is to become new paragraph (b).

* * * * *

Direct Participation Programs

Sec. 34.

[(a) A member or a person associated with a member shall not underwrite or participate in any way in the distribution to the public of units of a direct participation program, or sponsor a direct participation program, the provisions of which are inconsistent with rules, regulations and procedures prescribing standards of fairness and reasonableness in respect thereto adopted by the Board of Governors pursuant to the authorization granted in subsection (b) hereof.]

[(b) The Board of Governors is authorized, for the purpose of preventing fraudulent and manipulative acts and practices, promoting just and equitable principles of trade, providing safeguards against unreasonable profits or unreasonable rates of commissions or other charges, and for the protection of investors and the public interest, to adopt rules, regulations and procedures prescribing standards of fairness and reasonableness for direct participation programs relating to:]

[(1) the underwriting or other terms and conditions concerning, directly or indirectly, the distribution of units of such programs to the public, including, but not limited to, all elements of compensation in connection therewith, among other factors:]

[(2) the terms and conditions concerning the operations, structure and management of such programs in which a member or an affiliate of a member is a sponsor including, but not limited to:

a. the rights of participants in such programs;

b. conflicts or potential conflicts of interest of sponsors thereof, or others;

c. the financial condition of sponsors of such programs;

d. all elements of sponsor's compensation including but not limited to, working interests, net profit interests, promotional interests, program management fees, overriding royalty interests, sharing arrangements, interests in program revenues, and overriding interests of all other kinds, general and administrative expenses and organization and offering expenses;

e. the minimum unit value which

may be offered and the minimum subscription amount per investor;

f. the retention and/or exchange of units of the program held by participants;

g. the assessments, mandatory, optional or otherwise, to be made on participants in a program in addition to the unit price;

h. the reinvestment of revenues derived from the operation of the program;

i. the duty of the program to render operational and financial reports to participants;

j. the liquidation of units in a program; and

k. any other terms, conditions or arrangements relating to the operation of the program which the Board of Governors determines are required for the protection of investors and the public interest;]

[(3) the standards of suitability for investment in such programs by investors;]

[(4) the content and filing with the Association of advertising and sales

literature to be used in connection with the distribution of direct participation programs; and]

[(5) the definitions of words commonly used in connection with such programs including words used in this section unless they are otherwise defined herein.]

[(c) The rules, regulations and procedures authorized by subsection (b) hereof shall be incorporated into Appendix F to be attached to and made a part of these Rules of Fair Practice. The Board of Governors shall have the power to adopt, alter, amend, supplement or modify the provisions of Appendix F from time to time without recourse to the membership for approval, as would otherwise be required by Article VII of the By-Laws, and Appendix F shall become effective as the Board of Governors may prescribe unless disapproved by the Securities and Exchange Commission.]

[(d)] (a) Text unchanged.

(b) [APPENDIX F]

The text of former Appendix F is to become part of new paragraph (b).

* * * * *

[Operating Rules for ITS/CAES and CAES]

[Sec. 37. The Board of Governors is authorized to adopt rules, regulations and procedures required for the operation of the Computer Assisted Execution System including rules, regulations and procedures required for implementation of the linkage of the Computer Assisted Execution System and the Intermarket Trading System and the Intermarket Trading System Plan pursuant to which that linkage was consummated. The rules, regulations and procedures adopted hereunder shall be entitled "CAES Operating Rules" or "ITS/CAES Operating Rules" as the case may be. The Board of Governors shall have the power to alter, amend, supplement or modify the provisions of these rules, regulations and procedures from time to time without recourse to the membership for approval as otherwise would be required by Article VII of the By-Laws.]

NASD NOTICE TO MEMBERS 93-16

SEC Approves Code of Procedure Amendments That Permit the NASD to Institute Summary Revocation Proceedings For Failing to Pay an Arbitration Award

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On January 26, 1993, the Securities and Exchange Commission (SEC) approved an amendment to Article VI, Section 3 of the NASD By-Laws that permits the NASD to institute revocation proceedings against any member or associated person that fails to pay an arbitration award rendered by an NASD panel if a timely motion to vacate or modify the award has either not been filed or has been denied. The text of the amendment follows this Notice.

Background

In recent years, disciplinary actions involving failure to pay arbitration awards have congested the disciplinary dockets of the NASD's District Business Conduct Committees. Accordingly, the NASD has amended the By-Laws to permit initiation of revocation proceedings against members and associated persons that fail to pay arbitration awards rendered by an NASD arbitration panel.¹ The amendment took effect when the SEC approved it on January 26, 1993.

Currently, the NASD's Code of Arbitration Procedure contains a Resolution of the Board of Governors (Resolution) (paragraph 3744, page 3726 of the *NASD Manual*) that says failure to pay an arbitration award properly rendered by any one of several arbitration forums may be deemed "conduct inconsistent with just and equitable principles of trade and a violation of Article III, Section 1 of the Rules of Fair Practice" of the NASD. The Resolution contemplates a disciplinary action against a member firm or associated person for failing to pay an arbitration award rendered by the NASD; another

self-regulatory organization administering the Securities Industry Conference on Arbitration's Uniform Code; or the American Arbitration Association.

The NASD routinely brings disciplinary action for failing to pay arbitration awards when such violations are discovered through referrals from the NASD's Arbitration Department or other NASD departments; through referrals from other self-regulatory organizations; through routine or non-routine investigations; or through customer complaints. In 1991, the Arbitration Department referred 122 cases to the NASD's district offices for investigation of failure to pay an arbitration award rendered in the NASD's arbitration forum. In 1990, the Arbitration Department referred 82 such cases.

The amendment permits the NASD to employ its revocation procedures under Article VI of the Code of Procedure if a member or associated person fails to pay an arbitration award rendered by an NASD arbitration panel where a timely motion to vacate or modify the arbitration award has either not been filed or has been denied. Under Article VI of the Code of Procedure, the NASD will notify the member or associated person at least 15 days before the effectiveness of the proposed revocation. The member or associated person may file a written request for a hearing that must be received by the NASD before the expiration of the 15-day notice period. In the event a hearing is requested, a hearing panel designated by the NASD will hear the matter. Any decision rendered by such a hearing panel will constitute final NASD action and any revocation

¹The proposed amendment was published for member vote in *Notice to Members 92-1* (January 1992).

will be effective on a date established by the panel.

While Article VI, Section 3 of the Code of Procedure provides that a respondent in such a hearing is entitled to present “any relevant matter,” the arbitration proceeding and award which formed the basis for the revocation proceeding will not be subject to review or collateral attack. Such review or collateral attack may only be had pursuant to a timely motion to vacate or modify the arbitration award in accordance with applicable law made before a court of competent jurisdiction. Therefore, the only relevant matters before a panel in a revocation proceeding will be to determine if the award was validly issued pursuant to the rules of the arbitration forum and if it has been paid. The existence of a settlement agreement

between the parties to the arbitration proceeding calling for the payment of the award, provided the agreement is not in default, may be relevant to the issue of payment in such a proceeding.

Questions concerning this Notice may be directed to the NASD’s Arbitration Department at (212) 480-4881.

**Amendment to Article VI,
Section 3 of the NASD By-Laws**

(Note: New text is underlined; deleted text is bracketed.)

**Suspension of Cancellation of
Membership or Registration
[for Non-Payment of Dues]**

Sec. 3. The Corporation after fifteen

(15) days notice in writing, may suspend or cancel the membership of any member or the registration of any person in arrears in the payment of any fees, dues, assessments or other charges, or for failure to furnish any information or reports requested pursuant to Section 2 of this Article, or for failure to comply with an award of arbitrators properly rendered pursuant to Section 41 of the Code of Arbitration Procedure, where a timely motion to vacate or modify such award has not been made pursuant to applicable law or where such a motion has been denied.

NASD NOTICE TO MEMBERS 93-17

SEC Approves Changes To Uniform Practice Code Establishing Close-Out Procedures for Fails

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On January 14, 1993, the Securities and Exchange Commission (SEC) approved amendments to Sections 59 and 65 of the NASD's Uniform Practice Code (UPC) establishing close-out procedures for instruments based on the performance of an index, currency, or other measure and establishing close-out and fail procedures to be used in customer account transfers. The text of these amendments, (along with sample forms), which take effect March 1, 1993, follow this Notice.

Background

The amendment to Section 59 of the UPC establishes fail-to-deliver and liability-notice procedures for foreign currency and index warrants and other similar instruments.¹ These instruments may be exercised at any time and do not provide for a guaranteed post-expiration period for the buyer to deliver the physical certificates. Moreover, because the decision to exercise these instruments is based on the performance of a currency, index, or other standard, the buyer's exercise instruction to the agent may occur at any time and cannot be delayed. Because the buyer of foreign currency and index warrants has no protection under current UPC liability rules, the NASD has amended Section 59 to initiate a liability-notice procedure for these types of instruments. The amendment permits immediate origination and retransmission of liability notices, requires that the liability notice be written or transmitted through an electronic device having immediate receipt capabilities, requires mutual consent before cancellation of a liability notice, and cautions members to retain documentation relating to exercise requests. Sample forms relating to

liability notification will be included in the *NASD Manual* following Section 59 and are included in this Notice following the new rule language.

Section 65 of the UPC establishes procedures for timely processing of customer account transfers. Section 65(c) currently makes account transfers dependent on the disposition of "non-transferable assets," which are separately defined. The amendment to Subsection 65(c) adds new categories of nontransferable assets such as foreign securities, baby bonds, and certain limited partnerships. Further, the amendments clarify the members' responsibility to resolve and reverse transfers of improperly identified assets and requires members to update their records and notify customers of such action.

Subsections 65(d) through (f) have also been amended to clarify their application. Subsection 65(d)(1), which requires members to freeze accounts and cancel open orders upon validation of transfer instructions, has been amended to exempt options positions that expire within seven days. Subsection 65(d)(3), which permits a member receiving a transfer instruction to take exception under certain circumstances, has been expanded to include: the lack of transferrable assets in the account; an incorrect account number; and duplicative requests. If the transfer request is rejected because the account reflects no transferrable assets, the requesting or receiving member may not retransmit the request without attaching a copy of the customer's most recent account statement.

¹Such warrants are also known as American style warrants, in contrast to European style warrants that can only be exercised during a specified period before the warrant expires.

Subsection 65(e), which relates to the completion of a transfer, has been amended to delete the reference to options positions. This amendment recognizes that options positions are not deliverable instruments and, therefore, buy-in, close-out, and fail-to-deliver procedures do not apply to such positions. Rather, as a result of the direct interface between the National Securities Clearing Corporation (NSCC) and the Options Clearing Corporation (OCC), open options positions in a customer account subject to a transfer instruction are transmitted through NSCC to OCC for settlement. Thus, the reference in Subsection 65(e) to options is unnecessary.

Subsection 65(f), which relates to the establishment of fails resulting from account transfers, has been amended to require members to promptly resolve such fails in accordance with all applicable close-out and liability procedures. The subsection has also been amended to provide that the requirement to clearly identify such fails does not apply to a fail that is entered into a repricing and reconfirmation service and that emerges from such service without settling. Any fail that emerges from such a service without settling will continue to be a fail subject to all applicable rules.

Subsection 65(g), which relates to the resolution of discrepancies in transferred accounts, has been expanded to require the prompt transfer or distribution of assets that accrue (i.e., dividends, bond interest) to the customer's account after the initial transfer has been completed.

Subsections 65(h) and (i) have been added to establish close-out and sell-out procedures for fails in instruments that do not currently

have such procedures (i.e., zero-coupon bonds, mutual funds, limited partnerships). The amendments provide a means of closing-out or selling-out fails in certain instruments that previously had remained outstanding for extended periods of time. Such unresolved fails have, on occasion, prevented accounts from transferring completely.

New Subsection 65(h), which relates to close-out procedures for fails that the carrying member has not settled, adds procedures to permit the receiving member to close the fail not sooner than the third business day following the delivery due date pursuant to required written notification. This new subsection also permits redelivery of a notice, in the form of a retransmission, against any existing fail, regardless of its origin, to facilitate the completion of the transfer and greatly reduce the member's general fail file. These procedures are based on the buy-in rules set forth in Section 59.

New Subsection 65(i), which relates to sell-out procedures for certain fails that result from account transfers, adds notification and sell-out procedures to permit the carrying member to sell any and all securities due or deliverable in the best available market, where the receiving member failed to accept delivery or where a properly executed Uniform Reclamation Form, a depository generated rejection advice, or a valid Reversal Form is lacking.

Sample forms relating to close-outs and account transfers will be included in the *NASD Manual* following Section 65 and are included in this Notice following the new rule language.

Questions concerning this Notice may be directed to Dottie Kennedy,

NASD Operations Department at (212) 858-4340, or to Elliott R. Curzon, Senior Attorney, Office of General Counsel at (202) 728-8451.

Amendments to Sections 59 and 65 of the Uniform Practice Code

(Note: New text is underlined; deleted text is in brackets.)

Close-Out Procedure "Buying-in"

Sec. 59

* * * * *

Failure to Deliver and Liability Notice Procedures

(i)(1)(A) Text unchanged.

(B) If the contract is for a deliverable instrument with an exercise provision and the exercise may be accomplished on a daily basis, and the settlement date of the contract to purchase the instrument is on or before the requested exercise date, the receiving member may deliver a Liability Notice to the delivering member no later than 11:00 A.M. on the day the exercise is to be effected. Notice may be redelivered immediately to another member but no later than noon on the same day. Such notice must be issued using written or comparable electronic media having immediate receipt capabilities. If the contract remains undelivered at expiration, and has not been cancelled by mutual consent, the receiving member shall notify the defaulting member of the exact amount of the liability on the next business day.

(C) In all cases, members must be prepared to document requests for which a Liability Notice is initiated.

* * * * *

Customer Account Transfer Contracts

Sec. 65

* * * * *

Transfer instructions

(c)(1)

* * * * *

(C) With respect to transfers of securities accounts other than retirement plan securities accounts, the customer affirms that he or she has destroyed or returned to the carrying member any credit/debit cards and/or unused checks issued in connection with the account.

For purposes of this rule, a “non-transferable asset” shall mean an asset that is incapable of being transferred from the carrying member to the receiving member because it is:

(i) - (iv) Text unchanged.

(v) an asset that is an issue for which the proper denominations cannot be obtained pursuant to governmental regulation or the issuance terms of the product (e.g., foreign securities, baby bonds, etc.)

(vi) limited partnership interests in retail accounts.

(D) The carrying member and the receiving member must promptly resolve and reverse any nontransferable assets which were not properly identified during validation. In all cases, each member shall promptly update their records and bookkeeping systems and notify the customer of the action taken.

* * * * *

Validation of transfer instructions

(d)(1) Upon [receipt] validation of a transfer instruction, a carrying member must “freeze” the account to be transferred, i.e., all open orders, with the exception of option positions which expire within seven (7) business days, must be cancelled and no new orders may be taken.

(2) A carrying member may not take exception to a transfer instruction, and therefore deny validation of the transfer instruction, because of a dispute over securities positions or the money balance in the account to be transferred. Such alleged discrepancies notwithstanding, the carrying member must transfer the securities positions and/or money balance reflected on its books for the account.

(3) A carrying member may take exception to a transfer instruction only if:

(A) it has no record of the account on its books;

(B) the transfer instruction is incomplete; [or]

(C) the transfer instruction contains an improper signature[.];

(D) the account is “flat” and reflects no transferrable assets;

(E) the account number is incorrect; or

(F) it is a duplicate request.

If a carrying member takes exception to a transfer instruction because the account is “flat,” as provided in (D), the receiving member may re-submit the transfer instruction only if the most recent customer statement is attached.

* * * * *

Completion of the transfer

(e) Within five (5) business days following the validation for a transfer instruction, the carrying member must complete the transfer of the account(s) to the receiving member. The receiving member and the carrying member must immediately establish fail-to-receive and fail-to-deliver contracts at then-current market values upon their respective books of account against the long/short positions [(including options)] in the customer’s account(s) that have not been physically delivered/received and the receiving/carrying member must debit/credit the related money amount. The customer’s account(s) shall thereupon be deemed transferred.

Fail contracts established

(f)(1) Any fail contracts resulting from this account transfer procedure [must be closed out promptly.] shall be included in a member’s fail file and shall be promptly resolved according to applicable close-out and liability procedures.

(2) A carrying member may not reject (“DK”) a fail contract, including a Receive/Deliver Instruction [balance order] generated by an automated customer account transfer system, in connection with assets in an account transferred that have not been delivered to the receiving member.

(3) All fail contracts established pursuant to the requirements of this rule should be clearly marked or captioned as such. This subsection will not apply if a fail contract participates in a repricing and reconfirmation service offered by a registered clearing agency.

* * * * *

Prompt resolution of discrepancies

(g)(1) Text unchanged.

(2) The carrying member must promptly distribute to the receiving member any transferrable assets which accrue to the account after the transfer of a customer's securities account.

Close-out procedures

(h) A valued fail contract in a security, for which there are no established close-out procedures, and which has not been completed by the carrying member, may be closed by the receiving member no sooner than the third business day following the date delivery was due, in accordance with the following procedure:

(1) Written notice shall be delivered to the carrying member at his office not later than 12 noon, his time, two business days preceding the execution of the proposed "close-out".

(2)(A) Every notice of "close-out" shall state the settlement date, the quantity and contract price of the securities covered by said contract, and shall state further that unless delivery is effected at or before a certain specified time, which may not be prior to 3:00 P.M. local time in the community where the carrying member maintains his office, the security may be "closed-out" on the date specified for the account of the carrying member.

(B) Original notices may only be issued pursuant to fail contracts marked or captioned as fails established pursuant to subsection (f)(3) of this rule.

(C) Notice may be redelivered

immediately to another member from whom the securities involved are due in the form of a re-transmitted notice. A re-transmitted notice must be delivered to subsequent members not later than 12 noon one business day preceding the original date of execution of the proposed close-out.

(D) Re-transmitted notices may be issued against any fail contract regardless of its origin.

(3)(A) On failure of the carrying member to effect delivery in accordance with the notice, or to obtain a stay as hereinafter provided, the receiving member may close the contract by purchasing the securities necessary to complete the contract. Such execution will also operate to close-out all contracts covered under re-transmitted notices.

(B) The party executing the "close-out" shall immediately upon execution, but no later than the close of business, local time, where the seller maintains his office, notify the member for whose account the securities were bought as to the quantity purchased and the price paid. Such notification should be in written or electronic form having immediate receipt capabilities. If a medium with immediate receipt capabilities is not available, the telephone shall be used for the purpose of same day notification, and written or similar electronic notification having next day receipt capabilities must be sent out simultaneously. In either case formal confirmation of purchase along with a billing or payment (depending upon which is applicable) should be forwarded as promptly as possible after the execution of the "close-out". Notification of the execution of the "close-out" shall be given to succeeding members to whom a re-transmitted notice was

issued using the same procedures stated herein.

(C) If prior to the closing of a contract on which a "close-out" notice has been given, the receiving member receives from the carrying member written notice stating that the securities are 1) in transfer; 2) in transit; 3) being shipped that day; or 4) due from a depository and include the certificate numbers, then the receiving member must extend the execution date of the "close-out" for a period of seven (7) calendar days from the date delivery was due under the "close-out", except for those securities due from a depository.

(4) In the event that a "close-out" is not completed on the day specified in the notice, said notice shall expire at the close of business on the day specified in the notice, or if extended, at the close of business on the last day of the extension.

Sell-out procedures

(i)(1) Upon failure of the receiving member to accept delivery in accordance with the terms of the contract, and lacking a 1) properly executed Uniform Reclamation Form; 2) depository generated rejection advice; or 3) valid Reversal Form, the carrying member may, without notice, "sell-out" in the best available market, for the liability of the party in default, all or any part of the securities due or deliverable under the contract.

(2) The party executing a "sell-out" as prescribed above shall notify, no later than the close of business (local time where the receiving member maintains his office) on the day of execution, the member, for whose account and liability such securities were sold, of the quantity sold and the price received. Such notification should be in written or

electronic form having immediate receipt capabilities. A formal confirmation of such sale should be

forwarded as promptly as possible after the execution of the "sell-out".

(h) - (l) redesignated as (j) - (n).

SAMPLE FORMS

SAMPLE LIABILITY NOTICE

DATE: _____

TO: _____

RE: _____ (Quantity and Description of Security) CUSIP # _____

Reference is made to your obligation to deliver under a contract for the purchase of the above-referenced security entered into on _____ (Date of Contract) at _____ (Contract Price) for settlement on _____ (Settlement Date) _____. The security currently (is the subject of/permits the holder to) _____ (Specify tender/exchange offer, conversion, exercise of rights/warrants, etc.) _____. Pursuant to Section 59(i) of the NASD Uniform Practice Code, we hereby notify you that unless you make delivery of the foregoing security on or before (Time and Date) _____, we will hold you liable for any damages which may result. If you fail to deliver, damages are estimated at but not limited to _____.

NOTE: If some or all of the foregoing securities are due you by another member of the National Association of Securities Dealers, Inc., Section 59(i) permits the use of a Re-Transmitted Liability Notice.

(Member Firm)

(Official Signature)

If any questions, please contact:
(Name and Telephone Number)

SAMPLE RE-TRANSMITTED LIABILITY NOTICE

DATE: _____

TO: _____

RE: _____ (Quantity and Description of Security) _____ CUSIP # _____

Reference is made to your obligation to deliver under a contract for the purchase of the above-referenced security entered into on _____ (Date of Contract) at _____ (Contract Price) for settlement on _____ (Settlement Date) _____. The security currently (is the subject of/permits the holder to) _____ (Specify tender/exchange offer, conversion, exercise of rights/warrants, etc.) _____. Pursuant to Section 59(i) of the NASD Uniform Practice Code, we hereby notify you that a Liability Notice has been issued with respect to the referenced security. Unless delivery of the foregoing security is made on or before _____ (Time and Date of Original Notice) _____, we will hold you liable for any damages which may result. If you fail to deliver, damages are estimated at but not limited to _____.

NOTE: If some or all of the foregoing securities are due you by another member of the National Association of Securities Dealers, Inc., Section 59(i) permits the use of a Re-Transmitted Liability Notice.

(Member Firm)

(Official Signature)

If any questions, please contact:
(Name and Telephone Number)

SAMPLE NOTICE OF CLOSE-OUT

DATE: _____

TO: _____

RE: _____ (Quantity and Description of Security) _____ CUSIP # _____

The referenced security is due to be delivered by you to the undersigned pursuant to a Customer Account Transfer dated _____ at _____ (Contract Price) for settlement on _____ (Settlement Date). Pursuant to Section 65(h) of the NASD Uniform Practice Code, we hereby notify you that unless delivery of the foregoing security is made on or before _____ (Time and Date), the security will be closed-out for your account and risk.

NOTE: If some or all of the foregoing securities are due you by another member of the National Association of Securities Dealers, Inc., Section 65(h) permits the use of a Re-Transmitted Close-Out Notice.

(Member Firm)

(Official Signature)

If any questions, please contact:
(Name and Telephone Number)

SAMPLE NOTICE OF RE-TRANSMITTED CLOSE-OUT

DATE: _____

TO: _____

RE: _____ (Quantity and Description of Security) _____ CUSIP # _____

The referenced security is due to be delivered by you to the undersigned pursuant to a Customer Account Transfer made at _____ (Contract Price) for settlement on _____ (Settlement Date). Pursuant to Section 65(h) of the NASD Uniform Practice Code, we hereby notify you that a Notice of Close-out has been issued with respect to the referenced securities which stated that unless delivery of the foregoing security is made on or before _____ (Time and Date of Original Close-out), the security will be closed-out for your account and risk.

NOTE: If some or all of the foregoing securities are due you by another member of the National Association of Securities Dealers, Inc., Section 59(i) permits the use of a Re-Transmitted Close-Out Notice.

(Member Firm)

(Official Signature)

If any questions, please contact:
(Name and Telephone Number)

NO.

**BROKER NAME
ADDRESS
CITY, STATE, ZIP**

Telephone:

**DELIVERY TICKET FOR
CUSTOMER ACCOUNT TRANSFER**

The attached securities are delivered against payment.

Orig.No.	Del'd.via	Deliver Account No.	Trans.No.	Sett.Date	Del.Date
Customer Account Name/Type			Receiver Name and Address		
Receiver Account Number					
Quantity	CUSIP Number	Security Description		Value	

NASD NOTICE TO MEMBERS 93-18

SEC Approves *Collateralized Mortgage Obligations Advertising Guidelines* for Communi- cations With the Public

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On January 27, 1993, the Securities and Exchange Commission (SEC) approved the NASD's *Collateralized Mortgage Obligations Advertising Guidelines* (*Guidelines*). The *Guidelines* provide a framework for members to assess the accuracy and appropriateness of Collateralized Mortgage Obligations (CMO) advertising. The NASD's Advertising Regulation Department will use the *Guidelines* to evaluate CMO advertising submitted for review pursuant to Article III, Section 35 of the Rules of Fair Practice or Section 8 of the Government Securities Rules. The full text of the *Guidelines*, which are effective immediately, follows this Notice.

Background

As short-term interest rates have come down in recent years, the NASD has observed an increasing emphasis by member firms on sales of investment products that are alternatives to certificates of deposit (CDs) and government securities for investors seeking to maximize returns while maintaining a high degree of safety. Asset-backed securities, specifically collateralized mortgage obligations (CMOs), appear to be one of the leading alternatives being actively promoted. Substantiating this observed trend is the NASD Advertising Regulation Department's receipt of an increasing number of advertisements for review relating to CMOs. These advertisements generally emphasize high yields, safety, government guarantees, and liquidity allegedly associated with these securities, and frequently compare them with CDs.

Concurrent with the increase in the number of filings related to CMOs,

the NASD is receiving increasing numbers of complaints about CMO advertisements. In light of this trend, the NASD is concerned that the sales practices employed by members in retailing CMOs as alternatives to CDs or government securities imply that CMOs are the equivalent of such instruments in safety and guarantees of interest and principal. The NASD is also concerned about the suitability of CMOs for certain investors, the disclosure of risks, and other sales-practice abuses.

The NASD has taken a number of steps to address the issues relating to CMOs in addition to adopting the *Guidelines* contained herein. In the September 1991 edition of the *NASD Regulatory & Compliance Alert*, the NASD cautioned members about misleading CMO advertising and stated its position on various aspects of such advertising. In *Notice to Members 92-27* (May 1992) the NASD restated its previous pronouncement relating to CMO advertisements, and recommended that members adhere to several enumerated standards and file CMO advertisements with the NASD before use. Finally, on October 28, 1992, the SEC approved amendments to Article III, Section 35 of the Rules of Fair Practice and Section 8 of the Government Securities Rules to require members to file CMO advertisements with the NASD's Advertising Regulation Department before use.¹

CMO Advertising Guidelines

The *Guidelines* contained herein are complementary to, and complete, the previous actions taken by the NASD on CMOs. The *Guidelines* set forth extensive and

¹See *Notice to Members 92-59* (November 1992).

detailed standards for CMO advertisements. They will serve not only to govern advertising communications with potential customers, but will also augment the business conduct framework for all communications and sales practices relating to CMOs.

The *Guidelines* contain General Considerations relating to Product Identification, Safety Claims, Claims About Government Guarantees, Simplicity Claims, and Claims About Predictability. The *Guidelines* also contain standards relating specifically to print advertising, including a standardized CMO advertisement, and standards for radio and television advertising.

For example, under Product Identification, the *Guidelines* warn against comparing CMOs to other products. Under Claims About Government Guarantees, the *Guidelines* emphasize that referring to CMOs as “government guaranteed” is probably misleading, even if the collateral is guaranteed, unless the CMO itself is guaranteed by a government agency. Finally, under Claims About Predictability, the *Guidelines* caution that it is misleading to state that the yield and average life of a CMO are assured.

The NASD believes that CMOs are complex investment vehicles and communications must fully and fairly disclose all material aspects of CMOs to avoid misleading investors. Further, in the NASD’s view all CMOs are not equal, and it is difficult to distinguish between them based on the content of an advertisement. Therefore, communications about CMOs should disclose all information necessary to show the features of the particular CMO being promoted. For example, two CMOs might have the same underlying collateral, yet

differ greatly in their likely prepayment rates — the so-called “prepayment assumptions.” Further, the advertisement of a CMO yield alone could be misleading without extensive disclosure, such as illustrations showing that yield predictions vary greatly if differing prepayment assumptions, average life, and maturities are used. Finally, terms such as “interest only CMO” or “principal only CMO” are usually not adequately explained in advertisements and should be avoided unless adequate discussion and disclosure is included.

Standardized CMO Advertisement

The *Guidelines* also provide a standardized CMO advertisement for print advertising that permits members to advertise CMO yields and sets forth the information the NASD deems necessary to prevent the communication from being misleading. Members are not required to use the standardized advertisement; however, members using a non-standardized format should provide the same information and comply with the same conditions as the standardized advertisement. A copy of the standardized advertisement follows the *Guidelines* at the end of this Notice.

Among the features of the standardized advertisement are: 1) essential information (coupon rate, anticipated yield/average life, specific tranche, final maturity date, and underlying collateral); 2) a disclosure statement indicating that the yield and average life are based on certain prepayment assumptions that may not be realized; 3) optional product features; and 4) broker/dealer information. The *Guidelines* require that the information in items 1 and 2 appear in all CMO advertising, while item 3 is

optional and item 4 may be tailored to the member’s preference.

Among the most important of the *Guidelines* for print advertisements, whether a member uses the standardized advertisement or its own, are the standards relating to statements of the yield and average life. They require that the statements of yield and average life be based on consensus prepayment assumptions from a nationally recognized service, such as Bloomberg, or the member must be able to justify the assumption used. This standard is designed to prevent advertisements which mislead investors by relying on unrealistic or excessively optimistic yield and average-life projections. Finally, the *Guidelines* also require the disclosure of the specific tranche so that investors may evaluate the quality and characteristics of the security and underlying collateral, features that are unique to each CMO.

Radio/Television Advertising

Finally, the *Guidelines* set forth standards for radio and television advertising. Because radio and television advertising is subject to much more variability than print advertising, the NASD has not attempted to develop a standardized format. Instead, the *Guidelines* require that all radio and television advertising contain certain statements or information, including: an oral notice recommending that interested individuals contact their representative for information on CMOs and how CMOs react to certain market conditions; an oral notice regarding prepayment assumptions identical to that required for print advertisements; and, standard information on the CMO being advertised (coupon rate, anticipated yield, average life, final maturity date, specific tranche, underlying collateral and, if appli-

cable, accrual bond disclosure).

The *Guidelines* will be published in the *NASD Manual* following Article III, Section 35 of the Rules of Fair Practice. Questions concerning this Notice may be directed to the NASD's Advertising Regulation Department at (202) 728-8330, or to Elliott R. Curzon, Senior Attorney, Office of General Counsel at (202) 728-8451.

Guidelines Regarding Communications With the Public About Collateralized Mortgage Obligations (CMOs)

1. General Considerations

In order to prevent a communication about CMOs from being false or misleading, there are certain factors to be considered, including, but not limited to, the following.

Product Identification

In order to assure that investors understand exactly what security is being discussed, all communications concerning CMOs should clearly describe the product as a "collateralized mortgage obligation." Member firms should not use proprietary names for CMOs as they do not adequately identify the product.

To prevent confusion and the possibility of misleading the reader, communications should not contain comparisons between CMOs and any other investment vehicle, including Certificates of Deposit.

Safety Claims

A communication should not overstate the relative safety offered by the CMO. Although CMOs generally offer low investment risk, they are subject to market risk like all

investment securities and there should be no implication otherwise. Accordingly, references to liquidity should be balanced with disclosure that, upon resale, an investor may receive more or less than his original investment.

Claims About Government Guarantees

Communications should accurately depict the guarantees associated with CMO securities. For example, in most cases it would be misleading to state that CMOs are "government guaranteed" securities. A government agency issue could instead be characterized as government agency backed. Of course, private-issue CMO advertisements should not contain references to guarantees or backing, but may disclose the rating.

If the CMO is offered at a premium, the communication should clearly indicate that the government agency backing applies only to the face value of the CMO, and not to any premium paid. Furthermore, communications should not imply that either the market value or the anticipated yield of the CMO is guaranteed.

Simplicity Claims

CMOs are complex securities and require full, fair and clear disclosure in order to be understood by the investor. A communication should not imply that these are simple securities that may be suitable for any investor seeking high yields. All CMOs do not have the same characteristics and it is misleading to indicate otherwise. Even though two CMOs may have the same underlying collateral, they may differ greatly in their prepayment speed and volatility.

Claims About Predictability

A communication would be misleading if it indicated that the anticipated yield and average life of a CMO were assured. It should disclose that the yield and average life will fluctuate depending on the actual prepayment experience and changes in current interest rates.

2. Print Advertising

Educational advertising, discussing generally the features of CMOs, can be a very useful and informative tool in explaining these securities to the investing public. However, such "generic" advertising should not contain anticipated yields or coupon rates.

Advertising relating to CMOs must be filed with the NASD's Advertising Department for review at least ten days prior to use, pursuant to requirements in Article III, Section 35 of the NASD Rules of Fair Practice and Section 8 of the NASD Government Securities Rules (NASD Rules).

The NASD has developed a standardized CMO yield advertisement that provides information deemed necessary to prevent the communication from being misleading. Members must file the standardized advertisement, ten days prior to its first use, with the NASD Advertising Department.

Members are not *required* to use the standardized advertisement. If firms do not elect to use the standardized advertisement, they should ensure that their advertising contains the same information and meets the same conditions as the standardized advertisement. Members using a non-standardized format must file the advertisement ten days prior to first use.

After an advertisement has been

filed prior to initial use, subsequent use of the *identical* advertisement, changed only to reflect the updated information for the security being advertised, does not require re-filing with the NASD. Such advertisements must be approved by a principal (or designee) and maintained in the member firm's files as required by NASD Rules.

Standardized CMO Advertisement

The standardized advertisement contains four sections, each of which must be given an equal portion of space in the ad. The information in Sections 1 and 2 is required to be included in advertising for CMOs. The information suggested for Section 3 is optional; therefore, the member may elect to include any, all or none of this information in the advertisement. The information in Section 4 may be tailored to the member's preferred signature.

An example of the standardized format may be found at the end of these Guidelines.

Section 1:

- Title — Collateralized Mortgage Obligations
- Coupon Rate
- Anticipated Yield/Average Life
- Specific Tranche — Number & Class
- Final Maturity Date
- Underlying Collateral

Section 2

• Disclosure Statement: "The yield and average life shown above consider prepayment assumptions that may or may not be met. Changes in payments may significantly affect yield and average life. Please contact your representative for information on CMOs and how they react to different market conditions."

Section 3

- Product Features (**Optional**):
- Minimum Denominations
- Rating Disclosure
- Agency/Government Backing
- Income Payment Structure
- Generic Description of Tranche (e.g., PAC, Companion)

Section 4

- Company Information:
- Name, Address, Telephone Number, Representative's Name, Memberships

If this standardized advertisement is used, the following conditions must also be met:

1. All figures in Section 1 must be in equal type size.
2. The disclosure language in Section 2 may not be altered and must be given equal prominence with Section 1.
3. The prepayment assumption used to determine the advertised yield and average life must either be obtained from a nationally recognized service (e.g., Bloomberg, Telerate) or the member firm must be able to justify the assumption used. A copy of either the service's listing for the CMO or the firm's justification must be attached to the copy of the ad that is maintained in the firm's advertising files in order to verify that the prepayment scenario advertised is reasonable and to satisfy the conditions for waiving the pre-use filing requirement.
4. If a member intends to impose a sales charge, a reasonable sales charge should be reflected in the anticipated yield.
5. The advertisement must include language stating that the security is "offered subject to prior sale and price change." This language may be included in any one of the four

sections.

6. If the bond advertised is an accrual bond, the following language should be included in Section 1:

"This is an accrual bond and may not currently pay principal and interest."

7. If the bond is being offered at par, the advertisement may include the yield to maturity in Section 1.

No additional information may be included in the standardized advertisement.

3. Radio/Television Advertising

Radio and television advertising alternatives are too varied to attempt to provide standardized formats for either medium. Such advertisements must be filed with the NASD at least ten days prior to first use. The storyboard or other description should accompany the filing of a television ad.

If an advertisement is filed with the NASD prior to its initial use, it is not necessary to subsequently refile the advertisement if the only changes are to update the information relating to the security being advertised. A copy of each advertisement should be approved by a principal (or designee) and should be maintained, along with a copy of the listing for the CMO or the firm's justification, in the member firm's files in accordance with NASD Rules.

The following guidelines should be followed when developing radio and television advertisements:

1. The advertisements must be preceded by the following oral disclaimer: "The following is an advertisement for Collateralized

Mortgage Obligations. Contact your representative for information on CMOs and how they react to different market conditions.”

2. The advertisements must disclose the information contained in the first section of the prototype print ads:

Coupon Rate, Anticipated Yield, Average Life, Final Maturity Date, Initial Issue Tranche (Number and Class), and Underlying Collateral.

3. The advertisements must contain the following oral disclosure statement:

“The yield and average life consider prepayment assumptions that may or may not be met. Changes in payments may significantly affect yield and average life.”

4. The advertisements must state that the CMO is “offered subject to prior sale and price change.”

5. If a member intends to impose a

sales charge, a reasonable sales charge should be reflected in the anticipated yield.

6. If the bond advertised is an accrual bond, the following language should be included:

“This is an accrual bond and may not currently pay principal and interest.”

7. If the bond is being offered at par, the advertisement may include the yield to maturity.

Collateralized Mortgage Obligations

8.50% Coupon

8.75% Anticipated Yield to 10-Year Average Life

FNMA 9532X, Final Maturity March 2010

Collateral 100% FNMA 8.50%

*The yield and average life shown above
consider prepayment assumptions that may or may not be met.
Changes in payments may significantly affect yield and average life.
Please contact your representative for information
on CMOs and how they react to different market conditions.*

\$5,000 Minimum

Income Paid Monthly

AAA (Implied Rating)/V-1 (Fitch Volatility Rating)

U.S. Gov't Agency Backed

Generic Description (e.g., PAC, Companion, Sequential Pay Bonds)

**Company Name
Contact Person
Address
City, State, ZIP Code
Phone Number**

Offered subject to prior sale and price change.

Member SIPC

NASD NOTICE TO MEMBERS 93-19

NASD Reminds Members to Settle Syndicate Accounts Within 90 Days of the Settlement Date

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD is reminding members that Section 66 of the NASD Uniform Practice Code (UPC) requires syndicate managers to settle syndicate accounts within 90 days of the syndicate settlement date. Members are, therefore, reminded to mail or, where appropriate, deliver checks to syndicate participants no later than the 90th day following settlement of the syndicate account. The relevant portion of the text of Section 66 follows this Notice.

Background

Section 66 of the UPC requires the syndicate manager to make final settlement of syndicate accounts within 90 days of the syndicate settlement date.

It has come to the attention of the NASD that some syndicate managers are engaging in practices that flout the intent of Section 66. Syndicate members have reported receiving payments several days or weeks later than the 90th day but dated as of the 90th day. These circumstances suggest that syndicate managers are engaging in practices that effectively delay final payment of syndicate participants beyond the 90th day in circumvention of Section 66.

The NASD reminds members that the intent of Section 66 is to ensure that final settlement of syndicate accounts occur not later than the 90th day after the syndicate settlement date. The NASD believes that compliance with Section 66 mandates that syndicate managers mail or, where appropriate, deliver checks to syndicate participants no later than the 90th day following settlement of the syndicate account. Section 66 serves to set an outside

limit on settlements. Members, however, are encouraged to settle accounts as quickly as possible.

The NASD also notes, however, that Section 2 of the UPC permits the Operations Committee to entertain a request for a delayed settlement date, under the Committee's authority to issue rulings concerning the operation of the Code, if final settlement on the 90th day is not possible due to extraordinary circumstances beyond the member's control.

Questions concerning this Notice may be directed to Elliott R. Curzon, Senior Attorney, Office of General Counsel, at (202) 728-8451.

Uniform Practice Code

Settlement of Syndicate Accounts

Sec. 66

(a) Definitions:

(1) "selling syndicate" means any syndicate formed in connection with a public offering to distribute all or part of an issue of corporate securities by sales made directly to the public by or through participants in such syndicate.

(2) "syndicate account" means an account formed by members of the selling syndicate for the purpose of purchasing and distributing the corporate securities of a public offering.

(3) "syndicate manager" means the member of the selling syndicate that is responsible for the maintenance of syndicate account records.

(4) "syndicate settlement date" means the date upon which

corporate securities of a public offering are delivered by the issuer to or for the account of the syndicate members.

(b) Final settlement of syndicate accounts shall be effected by the

syndicate manager within 90 days following the syndicate settlement date.

(c) No later than the date of final settlement of the syndicate account, the syndicate manager shall provide

to each member of the selling syndicate an itemized statement of syndicate expenses

* * * * *

NASD NOTICE TO MEMBERS 93-20

NASD and Other SROs Launch Continuing Education Effort for Member Firms

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD and five other securities industry self-regulatory organizations (SROs) have agreed to develop a single continuing education program for all securities industry registered representatives and principals. Furthermore, the NASD has agreed to remain flexible over the question of whether an assessment component should be included in any continuing education program. An 11-person task force will report back to the six SROs by mid-year with recommendations for implementing the program.

Background

The NASD Board of Governors, which originally authorized its Membership Committee to develop a continuing education program in July 1991, also agreed to calls from SROs to approach with an open mind any findings of an industry-wide task force recently formed to detail such a plan. In a resolution approved in early January of this year, the Board agreed to "be flexible with regard to an assessment component being a requirement of the continuing education program and that the NASD will reserve final judgment on this matter pending receipt of the recommendations of an industry task force to be formed"

The 11-person industry task force met initially on March 15, 1993 in New York City to review information gathered by the SROs and to develop the continuing education program. By working together, the SROs hope to avoid multiple state or SRO continuing education requirements, which might create an inefficient and unnecessary burden on members. The members of the industry task force are: Mary Alice Brophy, First Vice President

and Director of Compliance, Dain Bosworth Inc.; Ronald E. Buesinger, Corporate Secretary and Senior Vice President, A.G. Edwards & Sons, Inc.; Elena Dasaro, Compliance Official, H.C. Wainwright & Co., Inc.; Sheldon Goldfarb, Deputy General Counsel, Goldman Sachs; John P. Gualtieri, Vice President and Insurance Counsel, Prudential Insurance Company of America; Therese Haberle, Vice President, Fidelity Securities; Stephen Hammerman, Vice Chairman, Merrill Lynch, Pierce, Fenner & Smith, Inc.; James Harrod, General Principal, Investment Representative—Training and Development, Edward D. Jones & Co.; Todd A. Robinson, Chairman and CEO, Linsco/Private Ledger Corp.; Richard C. Romano, President, Romano Brothers & Co.; William R. Simmons, Senior Vice President and Associate National Sales Director, Dean Witter Reynolds, Inc.

Expected to submit an interim report to the SROs by mid-year, the task force represents a cross section of the securities industry and will solicit input from a wide range of members and other interested persons—including state regulators—through the North American Securities Administrators Association. When it reports back to the SROs, the task force is expected to:

- Review already-developed information by SROs on continuing education.
- Review the need for a continuing education program for securities industry professionals.
- Review information on continuing education programs already under study by state securities regulators and consider state requirements in the design and implementation of

any such SRO program for the securities industry.

- Define the nature and scope of any such continuing education program for securities industry professionals.
- Determine the appropriateness of adding an assessment for such a program.
- Develop an action plan for designing and implementing such a program.

Because of the complexity of today's products and markets, the SROs—including the New York Stock Exchange, American Stock Exchange, Philadelphia Stock Exchange, Chicago Board Options Exchange, and the Municipal Securities Rulemaking Board—agreed that there may be a need for a formal, industry-wide continuing education program to keep industry professionals up to date on prod-

ucts, markets, and rules while ensuring investor confidence in the securities industry.

Original Recommendations

The NASD Board of Governors in July 1991 originally authorized the NASD Membership Committee to develop a continuing education program for registered personnel that included either an in-house, NASD-approved assessment capability at individual firms or a required periodic assessment by the NASD.

Notice to Members 91-50 in August 1991 explained the NASD view that SROs should take the lead in increasing standards of professionalism as financial markets become increasingly complex. Traditional continuing education programs, according to the NASD Qualifications Standards Subcommittee, were rejected

because they merely measure attendance rather than performance and fail to recognize the differing abilities needed within the securities industry.

The Membership Committee reported back to the Board of Governors in November 1991 its recommendations regarding the structure of the Continuing Education and Assessment Program. Besides determining that all representatives and principals should fall under the program, the Committee determined that any continuing education program should include some sort of assessment capability.

Members wishing to comment on any aspect of the continuing education programs may contact the NASD Qualifications & Membership Department at (301) 590-6693.

NASD NOTICE TO MEMBERS 93-21

Good Friday: Trade Date-Settlement Date Schedule

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

The Nasdaq Stock MarketSM and the securities exchanges will be closed on Good Friday, April 9, 1993. "Regular way" transactions made on the preceding business days will be subject to the settlement date schedule listed below.

<u>Trade Date</u>	<u>Settlement Date</u>	<u>Reg. T Date*</u>
April 1	8	13
2	12	14
5	13	15
6	14	16
7	15	19
8	16	20
9	Markets Closed	—
12	19	21

Brokers, dealers, and municipal securities dealers should use these settlement dates to clear and settle transactions pursuant to the NASD Uniform Practice Code and Municipal Securities Rulemaking Board Rule G-12 on Uniform Practice.

Questions regarding the application of these settlement dates to a particular situation may be directed to the NASD Uniform Practice Department at (212) 858-4341.

*Pursuant to Sections 220.8(b)(1) and (4) of Regulation T of the Federal Reserve Board, a broker/dealer must promptly cancel or otherwise liquidate a customer purchase transaction in a cash account if full payment is not received within seven (7) business days of the date of purchase or, pursuant to Section 220.8(d)(1), make application to extend the time period specified. The date by which members must take such action is shown in the column entitled "Reg. T Date."

NASD NOTICE TO MEMBERS 93-22

Nasdaq National Market®
Additions, Changes,
And Deletions as of
February 22, 1993

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
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As of February 22, 1993, the following 44 issues joined the Nasdaq National Market,® bringing the total number of issues to 2,998:

Symbol	Company	Entry Date	SOES Execution Level
PHSV	Physicians Health Svcs, Inc. (Cl A)	1/22/93	1000
CEGE	Cell Genesys, Inc.	1/26/93	500
BSRF	BioSurface Technology, Inc.	1/27/93	1000
CANXB	Cannon Express, Inc. (Cl B)	1/27/93	500
PNDR	Ponder Industries	1/27/93	1000
SHMN	Shaman Pharmaceuticals, Inc.	1/27/93	500
STCP	Stephan Co. (The)	1/27/93	1000
ABFSP	Arkansas Best Corp. (Ser A Cum)	1/28/93	1000
CBNKP	Community Bancorp, Inc. (7.25% Cum Conv Pfd B)	1/28/93	500
DFNR	D F & R Restaurants, Inc.	1/28/93	1000
KNFL	Kenfil Inc.	1/28/93	1000
OLGC	Orthologic Corp.	1/28/93	1000
SUNL	Sunrise Leasing Corporation	1/28/93	1000
COCN	CoCensys, Inc.	1/29/93	1000
HPRKZ	Hollywood Park, Inc. (Dep Shrs)	2/2/93	1000
NRND	Norand Corporation	2/2/93	500
SMAN	Standard Management Corp.	2/2/93	1000
AMFB	American Federal Bank, FSB	2/3/93	500
MATH	MathSoft, Inc.	2/3/93	1000
PWRS	Powersoft Corporation	2/3/93	1000
RCKY	Rocky Shoes & Boots, Inc.	2/3/93	1000
PRXM	Proxima Corporation	2/4/93	1000
CSPK	Chesapeake Energy Corporation	2/5/93	1000
GPTA	Gupta Corporation	2/5/93	1000
INDE	Independent Entmt. Group, Inc.	2/5/93	500
MDYN	Molecular Dynamics, Inc.	2/5/93	500
CTAL	Catalytica, Inc.	2/9/93	1000
CREE	Cree Research, Inc.	2/9/93	500
XLTCP	Excel Tech., Inc. (Ser 1 Conv Pfd)	2/9/93	500
IVBK	Intervisual Books, Inc.	2/9/93	1000
GLBL	Global Industries, Ltd	2/10/93	1000
PEBO	Peoples Bancorp Inc. (Ohio)	2/10/93	200
TIDED	Tide West Oil Company	2/10/93	1000
CYBX	Cyberonics, Inc.	2/11/93	1000
MLTN	Molten Metal Technology, Inc.	2/11/93	1000
ROUSP	Rouse Co. (The) (Ser A Conv Pfd)	2/11/93	1000
BMJFR	B.M.J. Financial Corp. (Rts 3/15/93)	2/12/93	500
CRYL	CryoLife, Inc.	2/12/93	1000
IECE	IEC Electronics Corp.	2/12/93	1000
JMAR	JMAR Industries, Inc.	2/12/93	1000
UEIC	Universal Electronics Inc.	2/12/93	1000
WATS	Watson Pharmaceuticals, Inc.	2/17/93	1000
ARGY	Argosy Gaming Company	2/18/93	500
PLDIF	Petersburg Long Distance Inc.	2/18/93	500

Nasdaq National Market Symbol and/or Name Changes

The following changes to the list of Nasdaq National Market securities occurred since January 22, 1993:

New/Old Symbol	New/Old Security	Date of Change
CANXA/CANX	Cannon Express, Inc.(Cl A)/Cannon Express, Inc.	1/27/93
GEMC/GEMC	Geriatric & Medical Companies, Inc./Geriatric & Medical Centers, Inc.	1/27/93
RSFC/RSFC	Republic Security Financial Corporation/Republic Savings Financial Corp.	1/28/93
ORPC/ORPCV	Orion Pictures Corporation/Orion Pictures Corp. (WI)	2/3/93
SFSL/SFSL	Security First Corp./Security Fed Sav & Loan Assoc of Cleveland	2/8/93
SYCM/SYCM	Sybron Chemicals Inc./Sybron Chemical Industries Inc.	2/8/93
NCELW/NCELW	Nationwide Cellular Service, Inc. (Wts 4/12/93)/Nationwide Cellular Service, Inc. (Wts 2/15/93)	2/9/93
WPIC/WPIC	WPI Group, Inc./Walker Power, Inc.	2/12/93

Nasdaq National Market Deletions

Symbol	Security	Date
FFMY	First Federal Savings & Loan Assoc. Fort	1/25/93
HIMG	Health Images, Inc.	1/27/93
CRII	Crest Industries, Inc.	1/28/93
NYBC	New York Bancorp Inc.	1/28/93
FFBS	FedFirst Bancshares Inc.	2/1/93
FCHT	First Chattanooga Financial Corp.	2/1/93
CRTQR	Cortech Inc. (Rts 94)	2/2/93
OSTN	Old Stone Corporation	2/2/93
OSTNO	Old Stone Corporation (Ser B 12% Pfd)	2/2/93
IFEIW	Imagine Films Entertainment, Inc. (Wts)	2/4/93
WAMUP	Washington Mutual Savings Bank (Ser A Pfd)	2/8/93
LFIN	Lincoln Financial Corp.	2/10/93
SHOZC	Millfeld Trading Co., Inc. (Wts Cl A)	2/12/93
CHKE	Cherokee, Inc.	2/17/93
ABIO	Applied Biosystems Inc.	2/19/93
RECPC	Receptech Corporation	2/19/93

Questions regarding this Notice should be directed to Mark A. Esposito, Supervisor, Market Listing Qualifications, at (202) 728-8002. Questions pertaining to trade reporting rules should be directed to Bernard Thompson, Assistant Director, NASD Market Surveillance, at (301) 590-6436.

NASD DISCIPLINARY ACTIONS

Disciplinary Actions Reported for March

The NASD® is taking disciplinary actions against the following firms and individuals for violations of the NASD Rules of Fair Practice; securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board. Unless otherwise indicated, suspensions will begin with the opening of business on Monday, March 15, 1993. The information relating to matters contained in this Notice is current as of the fifth of this month. Information received subsequent to the fifth is not reflected in this publication.

Firms Expelled, Individuals Sanctioned

T.T. Securities, Inc. (Danville, California) and **James Patrick Tolley (Registered Principal, Menlo Park, California)**. The firm was fined \$40,000 and expelled from NASD membership. Tolley was fined \$190,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that, in financing and/or refinancing of properties owned by limited partnerships previously underwritten by the firm, Tolley diverted loan proceeds to other limited partnerships that the firm sold without disclosure to the limited partners. Furthermore, the firm and Tolley diverted funds belonging to investors of one limited partnership to another limited partnership that the firm had underwritten.

In addition, the firm, acting through Tolley, sold units of limited partnerships offered on a best efforts "part or none" basis and received investor funds without depositing the monies into an escrow account.

Firms Suspended, Individuals Sanctioned

Halliday Capital, Inc. (Seattle, Washington) and **Scott Buchanan Halliday (Registered Principal, Seattle, Washington)** were fined \$5,000, jointly and severally. In addition, the firm was suspended from NASD membership for 30 days and Halliday was suspended from association with any NASD member as a general securities principal for 30 days. Also, Halliday must requalify by examination as a general securities principal or a direct participation programs principal. The sanctions were based on findings that the firm, acting through Halliday, effected securities transactions while failing to maintain its minimum required net capital.

Oxford Capital Securities, Inc. (New York, New York), **James Anthony Sehn (Registered Principal, Eaton's Neck, New York)**, and **Samuel Osei Asibey Forson (Registered Principal, Brooklyn, New York)**. The firm was suspended from NASD membership for one year, and Sehn and Forson were each suspended from association with any NASD member in any capacity for one year. The sanctions were based on findings that the firm, acting through Sehn and Forson, denied the NASD's staff access to any of the firm's books and records. In addition, Sehn and Forson failed to respond to NASD requests for information.

Firms Fined, Individuals Sanctioned

FirstMoney Securities Corporation (Memphis, Tennessee) and **James H. Beckemeyer (Registered Representative, Memphis, Tennessee)** were each fined

\$20,000, and Beckemeyer was suspended from association with any NASD member in any capacity for one week. The sanctions were based on findings that the firm, acting through Beckemeyer, executed certain U.S. Government agency securities transactions with public customers. However, the firm, acting through Beckemeyer, failed to disclose to the Board of Directors and senior officers that the prices were not reasonably related to the then current market price for the securities, a practice commonly referred to as adjusted trading. In addition, the firm, acting through Beckemeyer, failed to reflect on its books and records that the transactions were not effected at the prevailing market price and caused false and misleading confirmations to be mailed to customers.

Firms and Individuals Fined

Piper Jaffray, Inc. (Minneapolis, Minnesota) and **Daniel Francis Brotherton (Registered Principal, Bellevue, Washington)** submitted an Offer of Settlement pursuant to which the firm was fined \$35,000 and Brotherton was fined \$25,000. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm failed to create, maintain, or enforce adequate supervisory procedures. Specifically, the findings stated that the firm failed to ensure that Brotherton adequately supervised the sales activities of a registered representative.

Individuals Barred or Suspended

Theodore Allocca (Registered Representative, Huntington, New York) was barred from association with any NASD member in any capacity. The National Business

Conduct Committee (NBCC) imposed the sanction following an appeal of a District 10 District Business Conduct Committee (DBCC) decision. The sanction was based on findings that Allocca failed to pay a \$67,556.02 NASD arbitration award.

Allocca has appealed this action to the Securities and Exchange Commission (SEC), and the sanctions, other than the bar, are not in effect pending consideration of the appeal.

Billy Joe Altstatt, II (Registered Representative, San Mateo, California) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Altstatt failed to respond to NASD requests for information regarding customer complaints.

Edward Dallin Bagley (Registered Principal, Salt Lake City, Utah) was fined \$50,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following the appeal of a District 3 DBCC decision. The sanctions were based on findings that Bagley parked securities to circumvent District Surveillance Committee inventory limitations and its directives to be fully-disclosed. Specifically, Bagley caused fictitious stock transaction entries to be made on his member firm's books and records to allow the firm to maintain a minimum level of net capital. As a result of the above activity, Bagley caused the firm to conduct a securities business while failing to maintain its minimum required net capital. In addition, Bagley filed inaccurate FOCUS Parts I and II reports.

Charles Michael Banacos (Registered Representative,

Breckenridge, Colorado) was fined \$94,175 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Banacos recommended to a public customer the purchase of securities, represented to the customer that he was associated with a firm that was not registered with the NASD, and received from the customer a \$24,175 check intended for the purchase of the securities. Banacos failed to purchase any securities for the customer, cashed the check, and converted the money to his own use and benefit. Banacos also failed to respond to NASD requests for information.

Keith A. Bergner (Registered Representative, Lakewood, Colorado) was fined \$5,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following appeal of a District 3 DBCC decision. The sanctions were based on findings that Bergner failed to pay a \$31,733.34 NYSE arbitration award.

Richard L. Blackstock (Registered Representative, Aurora, Colorado) was fined \$5,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Blackstock failed to pay a \$7,250 NASD arbitration award.

David A. Bohnenkamper (Registered Representative, Palm Harbor, Florida) submitted an Offer of Settlement pursuant to which he was fined \$25,000, suspended from association with any NASD member in any capacity for one year, and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Bohnenkamper consented to the

described sanctions and to the entry of findings that he engaged in fraudulent activity by preparing false and misleading books and records for public customers' accounts. In addition, the NASD found that Bohnenkamper effected unauthorized transactions in the same accounts.

Richard J. Calta (Registered Representative, Phoenix, Arizona) was fined \$19,275 and suspended from association with any NASD member in any capacity for 10 business days. In addition, he must requalify by examination in any capacity in which he desires to act.

The sanctions were based on findings that, in violation of the Board of Governors' Free-Riding and Withholding Interpretation, Calta purchased shares of a "hot issue" for a restricted account. Moreover, Calta failed to disclose to his member firm that he had opened the aforementioned account with another member firm and continued to effect securities transactions in the account without notifying his firm.

James D. Clemmons, II (Registered Representative, Peoria, Illinois) was fined \$35,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Clemmons participated in private securities transactions while failing to give written notice of his intention to engage in such activities to his member firm. Clemmons also failed to respond to NASD requests for information.

William F. Coble (Associated Person, Silver City, New Mexico) was fined \$56,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Coble obtained \$6,000 from two insurance

customers, caused their endorsements to be forged on checks representing these funds without authorization, and failed to use the monies for the customers' benefit. In addition, Coble falsified books and records by causing insurance policies of the aforementioned customers to be changed without their authorization to an address where Coble accepted mail. Coble also failed to respond to NASD requests for information.

Eric Michael Diehm (Registered Representative, Tampa, Florida) was fined \$5,000 and barred from association with any NASD member in any capacity with the proviso that the bar may be removed upon payment of an arbitration award. The NBCC imposed the sanctions following an appeal of a District 7 DBCC decision. The sanctions were based on findings that Diehm failed to pay a \$750 arbitration award.

Diehm has appealed this action to the SEC, and the sanctions are not in effect pending consideration of the appeal. Furthermore, the SEC issued an order granting a stay of Diehm's bar. He thereafter paid the arbitration award; the bar was thus effective only from December 21, 1992 through February 8, 1993.

Praveen Diwan (Registered Representative, Enclave, New Delhi, India) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$50,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Diwan consented to the described sanctions and to the entry of findings that without the knowledge or consent of public customers, Diwan submitted forms requesting withdrawals of accumulated dividends totaling \$7,573.16 from the cus-

tomers' policies. Furthermore, the findings stated that he had the checks delivered to his locked mail slot at his branch office and thereafter deposited the funds into his personal checking account.

Thomas Lee Dussault (Registered Principal, Iselin, New Jersey) was suspended from association with any NASD member in any capacity for three days. The sanction was based on findings that Dussault failed to pay a \$1,361.75 NASD arbitration award.

Robert L. Eaton (Registered Representative, Kingsport, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for two weeks. Without admitting or denying the allegations, Eaton consented to the described sanctions and to the entry of findings that he executed five unauthorized transactions in the account of a public customer.

The findings also stated that Eaton engaged in unsuitable transactions and a practice known as switching. Specifically, the NASD found that he recommended and executed the liquidation of various mutual funds and the purchase of other mutual funds with similar investment objectives that cost the customers \$3,440.60 in additional sales charges. In addition, the NASD determined that Eaton failed to respond in a timely manner to NASD requests for information.

Thomas J. Falzani (Registered Principal, Somerdale, New Jersey) submitted an Offer of Settlement pursuant to which he was fined \$2,500 and suspended association with any NASD member in any principal capacity for three months. Without admitting or

denying the allegations, Falzani consented to the described sanctions and to the entry of findings that a member firm, acting through Falzani, failed to comply with the SEC's Customer Protection Rule by failing to act, or to act timely, to reduce its possession or control of customer full-paid and excess margin securities, or made deliveries that created or increased a deficiency.

The findings also stated that the firm, acting through Falzani, failed to comply with the SEC's Customer Protection Rule by failing to complete sale transactions effected for the accounts of public customers by "buying in" securities not delivered by the customers within 10 business days following the trade date or the expiration of any applicable extension of time.

In addition, the NASD found that the firm, acting through Falzani, failed to obtain amounts required for maintenance margin on a timely basis and failed to comply with the requirements of the Uniform Practice Code to validate transfer of account instructions within five business days. Furthermore, the NASD determined that the firm, acting through Falzani, effected short sales for customers in cash accounts and failed to cancel promptly or otherwise liquidate purchase transactions effected in cash accounts that had not been paid in full within seven business days following the trade, in violation of Regulation T of the Federal Reserve Board.

The findings also stated that the firm, acting through Falzani, violated Regulation T when it effected purchase transactions for cash accounts subject to "90 day freezes" when such accounts did not already have sufficient funds to pay for the transactions in full on

the trade date. Moreover, the findings stated that they further violated Regulation T when they made improper liquidations in margin accounts. Specifically, the margin calls were met by liquidation rather than by a transfer from the special memorandum account or by a deposit of cash, margin securities, exempted securities, or any combination thereof.

Murray H. Frankel (Registered Representative, New City, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$1,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Frankel consented to the described sanctions and to the entry of findings that during the course of a Series 7 Examination, he had notes with material relevant to the examination.

Juanito A. Go (Associated Person, Long Beach, California) was fined \$1,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that while taking a qualifications examination, Go had material used to prepare and assist individuals in taking the examination.

James M. Graybosch (Registered Principal, Jackson, Tennessee) was fined \$10,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 5 DBCC decision. The sanctions were based on findings that Graybosch failed to disclose to his member firm that he executed documents purporting to grant him power of attorney and discretionary power over the account of a public customer. Graybosch also forged the same

customer's name on 32 documents and executed unsuitable transactions in her account and that of her minor son. In addition, Graybosch failed to disclose to his member firm his ownership and controlling interest in a corporate entity because of his failure to keep current his Form U-4.

James Richard Hackett, Jr. (Registered Representative, Wadsworth, Ohio) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$20,000, barred from association with any NASD member in any capacity, and required to pay \$10,000 in restitution to his member firm. Without admitting or denying the allegations, Hackett consented to the described sanctions and to the entry of findings that he converted two customer checks totaling \$19,817.83.

Richard C. Harpole (Registered Representative, Rochester, New York) was fined \$65,000, barred from association with any NASD member in any capacity, and required to pay \$15,000 in restitution to a public customer. The sanctions were based on findings that Harpole misappropriated and converted customer funds totaling \$15,000 to his own use. In addition, he failed to respond to NASD requests for information.

Timothy Joseph Harrington (Registered Representative, Los Gatos, California) was fined \$309,772.43 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Harrington received from three public customers funds totaling \$239,772.43 for the purchase of securities but misappropriated and converted the proceeds to other uses. Harrington also failed to

respond to NASD requests for information.

Hassan Hashemian (Registered Principal, Torrance, California) was fined \$104,538.23 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 2 DBCC decision.

The sanctions were based on findings that Hashemian engaged in excessive trading in a public customer's account by recommending to the customer the purchase and sale of options and securities without having reasonable grounds for believing that such recommendations were suitable for the customer. In addition, Hashemian executed unauthorized transactions in customer accounts.

Michael A. Iwe, Jr. (Registered Representative, Chicago, Illinois) was fined \$25,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Iwe prepared and delivered to the public sales literature and an advertisement without obtaining prior approval by a registered principal of his member firm. Iwe also failed to respond to NASD requests for information.

Randy Blaine Johnson (Registered Representative, Ogden, Utah) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Johnson received a check on a matured insurance policy for delivery to a public customer and caused the check to be deposited into his personal bank account. Thereafter, he used the funds for his personal use.

Jay B. Kitchens (Registered Representative, New Philadelphia, Ohio) submitted an Offer of Settlement pursuant to which he was fined \$25,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Kitchens consented to the described sanctions and to the entry of findings that he misappropriated and converted to his own use \$6,081.49 in customer funds intended for the purchase of a fixed annuity.

Alexander Andrew Kusulos (Registered Representative, Mill Creek, Washington) submitted an Offer of Settlement pursuant to which he was fined \$30,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegation, Kusulos consented to the described sanctions and to the entry of findings that he received from public customers checks totaling \$23,000 for investment purposes and failed to remit the funds as instructed. Instead, Kusulos endorsed the checks and deposited the funds into an account in which he had a beneficial interest.

Furthermore, the NASD found that Kusulos filed an inaccurate and misleading Uniform Application for Securities Dealer Industry Registration (Form U-4) by failing to disclose certain information.

David J. Leyshon (Registered Representative, Hopewell, Virginia) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$2,500 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Leyshon consented to the described sanctions and to the entry of findings that he affixed signa-

tures purporting to be those of public customers to documents that he submitted to his member firm as genuine.

Jules B. Lipow (Registered Principal, Riverside, Connecticut), Irving Levine (Registered Representative, Woodmere, New York), and Howard R. Perles (Registered Representative, Staten Island, New York) submitted an Offer of Settlement pursuant to which Lipow was fined \$100,000 and barred from association with any NASD member in any capacity. Levine was fined \$15,000 and suspended from association with any NASD member in any capacity for 15 business days. Perles was fined \$5,000 and suspended from association with any NASD member in any capacity for five business days.

Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that Lipow entered into an illegal arrangement with the principal shareholder of a blind pool for an over-the-counter stock not listed on Nasdaq to transfer control of the management of the blind pool and its outstanding unregistered shares. To effect the transactions required to transfer control of the stock, the NASD found that Lipow created false books and records, including the establishment of nominee accounts at his member firm to receive these securities.

Once Lipow obtained control of the blind pool, the NASD determined that he planned to use this control to manipulate the price of the securities, to sell those securities to the public as freely traded stock at artificially high prices through his member firm's retail sales force, and to otherwise use this undisclosed control of the stock to his own advantage.

In relation to this scheme, the NASD also found that Lipow engaged in insider trading, failed to disclose the common control of a member firm with the issuer, improperly distributed equity securities issued by an affiliate of a member firm, and purchased securities of an issuer as the underwriter before completion of the distribution.

Moreover, the findings stated that Levine and Perles provided knowing and substantial assistance by facilitating this distribution of unregistered shares. Specifically, the NASD determined that Levine and Perles purchased shares of the common stock on a principal basis from another member firm and within minutes of such purchase, sold the same shares from the firm's proprietary account to a different member firm.

Gary B. Marshall (Associated Person, Fayetteville, Arkansas) was fined \$35,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Marshall failed to submit accurate information when making application for registration with the NASD. In addition, Marshall failed to respond to NASD requests for information.

Joni Lynn Merwin (Registered Representative, Aurora, Colorado) was fined \$15,000 and suspended from association with any NASD member in any capacity for 30 days. The sanctions were based on findings that Merwin executed unauthorized transactions in customer accounts and guaranteed another customer against loss to induce him to purchase securities.

Kenneth N. Morton (Registered Representative, Charlotte, Vermont) submitted an Offer of

Settlement pursuant to which he was fined \$20,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Morton consented to the described sanctions and to the entry of findings that he misappropriated to his own use and benefit insurance customer funds totaling \$12,073.27 without the customer's knowledge or consent. In addition, Morton failed to respond to NASD requests for information.

Manoj D. Motwani (Registered Representative, Bayside, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$20,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Motwani consented to the described sanctions and to the entry of findings that he converted five checks from a public customer's money market account to his own use without the customer's knowledge.

Valerie W. Nalley (Registered Representative, Louisville, Kentucky) submitted a Letter of Acceptance, Waiver and Consent pursuant to which she was fined \$1,000 and suspended from association with any NASD member in any capacity for one week. Without admitting or denying the allegations, Nalley consented to the described sanctions and to the entry of findings that she made journal entries transferring funds between her account and accounts of her family members without obtaining valid letters of authorization.

The findings also stated that in an effort to conceal the aforementioned activities, Nalley altered at least eight separate daily journal reports to prevent the branch manager from reviewing a

complete record of daily activity. In addition, the NASD determined that Nalley forged the signature of her mother on three separate letters of authorization and a change of address request. Furthermore, the NASD found that in an effort to expedite the disbursed funds to public customers, Nalley forged the signatures of co-workers to customer checks.

Ephram Touma Nehme (Registered Representative, Thousand Oaks, California) submitted an Offer of Settlement pursuant to which he was fined \$30,676.26 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Nehme consented to the described sanctions and to the entry of findings that, without the knowledge or consent of insurance customers, Nehme forged their signatures on disbursement request forms and cash surrender forms to facilitate the withdrawal of certain accumulated dividends. Furthermore, the NASD found that he also forged their signatures on new life insurance application forms and used the aforementioned funds to make premium payments on the new life insurance contracts without their consent. This activity generated commissions for Nehme totaling \$676.26.

Angelo Pastore (Registered Representative, Sayville, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$22,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Pastore consented to the described sanctions and to the entry of findings that without the knowledge or consent of an insurance customer, he requested two unauthorized loans

totaling \$1,300 against the customer's policy and used the funds to pay for an additional policy for the customer.

In addition, the NASD found that Pastore submitted a cash surrender request for \$549.43 on the policy of another insurance customer, cashed the check with the customer's forged endorsement, and used the proceeds to buy a money order that was placed in the customer's file.

Frank Lyon Polk, III (Registered Representative, New York, New York) submitted an Offer of Settlement pursuant to which he was fined \$27,500 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Polk consented to the described sanctions and to the entry of findings that he effected 15 unauthorized transactions in the accounts of 10 public customers.

J. Kenneth Powell (Associated Person, West Mifflin, Pennsylvania) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Powell consented to the described sanctions and to the entry of findings that he forged the signatures of insurance customers on requests to withdraw accumulated policy dividends and on a request to surrender the cash value of an insurance policy.

In connection with this activity, the NASD found that Powell also forged their endorsements and the endorsements of other insurance customers on checks totaling \$3,490.74 issued to them by Powell's member firm and deposited the funds with his firm to pay premiums.

Manuel S. Sandoval (Registered Representative, Pueblo, Colorado) was fined \$38,616 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Sandoval obtained from public customers funds totaling \$13,381.47 intended for investment purposes and \$235 in cash for the purchase of automobile insurance. However, these funds were neither used as intended nor returned to the customers.

Michael Schatten, III (Registered Representative, Forest Hills, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$62,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Schatten consented to the described sanctions and to the entry of findings that he misappropriated to his own use and purpose \$41,612 from the accounts of public customers without their knowledge or consent.

Andrew Scudiero (Registered Representative, Whitestone, New York) and **Robert Hollis Griffith (Registered Representative, Bay Shore, New York)** submitted an Offer of Settlement pursuant to which Scudiero was fined \$10,000, suspended from association with any NASD member in any capacity for seven months and 15 days, and suspended from association with any NASD member in any supervisory capacity for three years. Scudiero was also prohibited for three years from maintaining any proprietary interest in any NASD member other than a non-controlling interest in a member whose shares are publicly traded and are subject to the reporting requirements of Section 12 of the Securities and Exchange Act of 1934. In addition, Scudiero is

required to requalify by examination before acting in any capacity and must pay \$38,300 in restitution to public customers.

Griffith was fined \$7,500 and suspended from association with any NASD member in any capacity for two years. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that they conducted a securities business without proper registration with the NASD. The NASD also found that Scudiero and Griffith caused trades to be effected in the accounts of public customers without their knowledge, authorization, or consent. In addition, the NASD determined that Scudiero made a written guarantee to a public customer and failed to respond to NASD requests for information. Furthermore, the findings stated that Griffith refused to accept a public customer's sell order unless the customer agreed to purchase additional stock. Also, according to the findings, Griffith made misrepresentations to public customers that the price of a common stock would increase.

Maynard Matt Smith (Registered Representative, Bayside, New York) was fined \$50,000, barred from association with any NASD member in any capacity, and required to pay \$56,100 in restitution to a public customer, jointly and severally with other respondents. The sanctions were based on findings that Smith recommended the purchase of unregistered shares of a common stock to a public customer without having reasonable grounds for believing that the transaction was suitable for the customer given the customer's financial condition and investment objectives. Moreover, Smith failed to ensure that the customer's account was managed properly. In addition,

Smith shared in the customer's account by sending her a personal money order for \$822.50 as a dividend on her investment.

Florence Terrie Sommer (Registered Representative, New York, New York) submitted an Offer of Settlement pursuant to which she was fined \$50,000 and suspended from association with any NASD member in any capacity for 24 months. Without admitting or denying the allegations, Sommer consented to the described sanctions and to the entry of findings that, the purchase and sale of certain securities, she exercised discretion in a customer's account without approval and engaged in excessive trading in a customer's account. Furthermore, the findings stated that Sommer forged customer signatures to various documents, executed unauthorized transactions, deposited personal funds into customer accounts, made misrepresentations to customers, and falsified member firm documents.

Ann Marie Sonderman (Registered Representative, Lexington, Kentucky) was fined \$85,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Sonderman received from two public customers \$44,735 for investment purposes. Sonderman deposited the funds into her personal checking account and converted the monies to her own use and benefit without the customers' knowledge or consent. In addition, Sonderman failed to respond to NASD requests for information.

Frank O. Spampinato (Registered Principal, Lauderdale, Florida) and **Albert F. DeMange (Registered Principal, Coral Springs, Florida)**. Spampinato was fined \$50,000 and barred from

association with any NASD member in any capacity. DeMange was fined \$25,000, suspended from association with any NASD member in any capacity for six months, and barred from association with any NASD member in any principal capacity. The NBCC imposed the sanctions following appeal of a District 7 DBCC decision. The sanctions were based on findings that a former member firm, acting through Spampinato and DeMange, participated in a parking scheme wherein they engaged in non-bona fide month-end sales and re-purchases of the firm's municipal bond inventory to conceal its ownership and to avoid, for financial reporting and net capital purposes, the haircut required by the SEC.

In addition, the firm, acting through Spampinato, failed to maintain accurate books and records, filed materially inaccurate FOCUS Parts I and II reports, and failed to maintain its required minimum net capital. Furthermore, the firm, acting through Spampinato, failed to deposit customer subscription funds in a separate bank trust account or bank escrow account in a contingent offering of units.

Erick Peter Spronck (Registered Representative, Clinton, New Jersey) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was suspended from association with any NASD member in any capacity for two years. Without admitting or denying the allegations, Spronck consented to the described sanction and to the entry of findings that without the approval of his member firm, he solicited loans from public customers and promised to pay 10 percent interest in one year.

Michael Sebastian Toscano (Registered Representative, Fenton, Missouri) was fined

\$21,000, barred from association with any NASD member in any capacity, and required to pay \$423.99 in restitution to a public customer. The NBCC imposed the sanctions following appeal of a District 4 DBCC decision. The sanctions were based on findings that Toscano received from a public customer \$423.99 to be applied to life insurance premiums. Instead, Toscano deposited the funds into his personal bank account, thereby converting the monies to his own use and benefit. In addition, Toscano failed to respond to NASD requests for information.

Thomas E. Warren, III (Registered Representative, Tulsa, Oklahoma) was fined \$5,000, suspended from association with any NASD member in any capacity for two weeks, and required to requalify by examination as a general securities representative. The NBCC imposed the sanctions following appeal of a District 5 DBCC decision. The sanctions were based on findings that Warren failed to record accurate information on new account forms for four children. Specifically, Warren failed to record accurately the ages of the children; accepted third-party discretionary instructions from their mother; and failed to record the mother's authority as custodian to execute such transactions. By failing to record this information accurately, Warren aided and abetted the children's mother in misappropriating funds in the accounts.

In addition, Warren recommended and executed margin transactions in the aforementioned accounts without having reasonable grounds for believing that the creation of debit balances through the use of margin was suitable for the customers. This margin activity enabled the children's mother to withdraw funds in

excess of \$300,000 from their account that would not otherwise have been available to her.

Warren has appealed this action to the SEC, and the sanctions are not in effect pending consideration of the appeal.

Martin Wewerka (Registered Representative, El Cajon, California) was fined \$5,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Wewerka failed to pay a \$5,000 NASD arbitration award.

Moses Wilson, Jr. (Registered Principal, Detroit, Michigan) submitted an Offer of Settlement pursuant to which he was fined \$75,000 and barred from association with any NASD member in any capacity. In addition, he must pay \$32,991.57 in restitution to insurance customers.

Without admitting or denying the allegations, Wilson consented to the described sanctions and to the entry of findings that he received from insurance customers checks totaling \$53,991.57 intended for the purchase of an annuity policy and a life insurance policy. The NASD determined that Wilson failed to follow the customers' instructions, used only \$21,000 as instructed, and used the remaining \$32,991.57 for purposes other than to benefit the customers. The findings also stated that Wilson failed to respond to NASD requests for information.

Auldis E. Wright (Registered Representative, Richmond, Virginia) submitted an Offer of Settlement pursuant to which he was fined \$90,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Wright consented to the described

sanctions and to the entry of findings that he engaged in private securities transactions and failed to respond to NASD requests for information.

John F. Yakimczyk (Registered Representative, Parker, Colorado) was fined \$15,000 and suspended from association with any NASD member in any capacity for three business days. The SEC affirmed the sanctions following an appeal of a June 1991 NBCC decision. The sanctions were based on findings that Yakimczyk provided inaccurate quotations to public customers to conceal the fact that the securities were dropping in price, and failed to follow customer instructions to sell their stock. Yakimczyk also made unauthorized transactions in three customer accounts.

Agostino Joseph Zolezzi (Registered Principal, San Diego, California) was fined \$7,500, jointly and severally with a member firm, fined an additional \$500, jointly and severally with other respondents, and suspended from association with any NASD member in any capacity for three days. The NBCC imposed the sanctions following appeal of a District 2 DBCC decision.

The sanctions were based on findings that a member firm, acting through Zolezzi, effected securities transactions and/or induced the purchase or sale of securities when the firm failed to maintain sufficient net capital. In addition, the firm, acting through Zolezzi, failed to give telegraphic notice of its net capital deficiency in a timely manner and failed to file a report detailing steps taken to correct the situation. Furthermore, the firm, acting through Zolezzi, sold shares of an initial public offering to a public customer without a final

registration statement in effect and without the benefit of an exemption from registration, in violation of Section 5 of the Securities Act of 1933.

Zolezzi has appealed this action to the SEC and the sanctions are not in effect pending consideration of the appeal.

Individuals Fined

Joseph Simon Arsenault (Registered Representative, Manhasset, New York) submitted an Offer of Settlement pursuant to which he was fined \$12,000. Without admitting or denying the allegations, Arsenault consented to the described sanction and to the entry of findings that he effected unauthorized transactions in the accounts of public customers. In addition, the findings stated that Arsenault failed to disclose on his Form U-4 that he was the subject of customer complaints.

Emery E. Boudreau (Registered Principal, Oakton, Virginia) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$15,000. Without admitting or denying the allegations, Boudreau consented to the described sanction and to the entry of findings that he engaged in private securities transactions while failing to notify his member firm of such activity.

Paul Charles Hedrick (Registered Representative, Palm Beach Gardens, Florida) submitted an Offer of Settlement pursuant to which he was fined \$10,250. Without admitting or denying the allegations, Hedrick consented to the described sanctions and to the entry of findings that he effected sales of a common stock in a private placement offering to public

customers without providing written notification to or obtaining written authorization from his member firm.

Richard Kaye (Registered Representative, Long Beach, California) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000. Without admitting or denying the allegations, Kaye consented to the described sanction and to the entry of findings that he sold securities without being properly qualified and failed to notify his member firm of his association with another member firm.

Gregory Small (Registered Principal, Tierra Verde, Florida) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Small consented to the described sanctions and to the entry of findings that he effected unauthorized transactions in the securities accounts of public customers.

Stanley Zicklin (Registered Principal, Woodland Hills, California) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000. Without admitting or denying the allegations, Zicklin consented to the described sanction and to the entry of findings that, without written authorization from his member firm, he shared in loss-

es in the accounts of five public customers and made no financial contribution to the accounts.

Firm Expelled for Failure to Pay Fines and Costs in Connection With Violations

Equitrade, Incorporated,
Nashville, Tennessee

Firm Suspended

The following firm was suspended from membership in the NASD for failure to comply with formal written requests to submit financial information to the NASD. The action was based on the provisions of Article IV, Section 5 of the NASD Rules of Fair Practice and Article VII, Section 2 of the NASD By-Laws. The date the suspension commenced is listed after the entry. If the firm has complied with the requests for information, the listing also includes the date the suspension concluded.

Selective Security Trust Financial Corp., Braintree, Massachusetts
(February 5, 1993)

Suspensions Lifted

The NASD has lifted suspensions from membership on the dates shown for the following firms, because they have complied with formal written requests to submit financial information.

America/Southwestern Securities Group, Inc., Fort Worth, Texas
(January 26, 1993)

Lone Star Securities, Inc., Abilene, Texas
(January 29, 1993)

Viking Financial, Inc., Plano, Texas
(January 26, 1993)

Individual Barred for Failure to Comply With Sanctions Imposed

Andrew Scudiero, Whitestone, New York

Individuals Whose Registrations Were Revoked for Failure to Pay Fines and Costs in Connection With Violations

Brian T. Baker, St. Louis, Missouri

Jay M. Fertman, Castle Rock, Colorado

Brian P. Gentry, Glen Ellen, California

Richard C. Garton, Pittsburgh, Kansas

Eric F. Ho, Demarest, New York

Franklin J. Portier, Columbus, Ohio

Michael C. Saunders, Kansas City, Missouri

Jerry J. Turcan, Rye, New York

FOR YOUR INFORMATION

Major Medical Plan for Individuals Adjusts Rates in Most Cost Areas

Despite the national trend toward higher costs for medical coverage, our plan administrators report that premiums for the majority of those participating in the National Casualty HealthGuard Plus program will remain virtually the same as they have been since April 1992, and in many cases will be lower. Those in the high cost geographic areas, however, will experience some increase in keeping with the national trend.

In response to numerous requests, the Plan has added another deductible option of \$5,000 per calendar year — also available as of April 1 — and the premium discount for covering spouses will automatically increase from 10 percent to 15 percent, applicable to both insured and spouse.

Additionally, on April 1, 1993, the lifetime maximum benefit will double to \$2,000,000 and the maximum age for application for coverage will rise from 59 to 64. These changes reflect plan growth and the insurers' willingness to provide greatest possible flexibility.

For more information, call Benefits Administrators, Inc., at (800) 336-0883.

New Products Added to Series 7

The Series 7 examination will soon include questions on collateralized mortgage obligations (CMOs), long-term equity options, and capped index options. These products are not presently tested on the examination. The questions will be added to the pretest (unscored) group beginning April 12, 1993. After the pretest period, as early as May 12, 1993, acceptable questions

will be scored. The total number of questions selected for each topic area in the examination will remain unchanged.

Questions dealing with long-term equity options and capped index options will be included among the questions on exchange-traded equity options (section 4.7.2) and exchange-traded index options (section 4.7.3), respectively. The questions will test the candidate's knowledge of underlying securities, exercise settlement, and other basic product information.

CMOs will be given equal weight with other types of mortgage-backed securities included in the content outline (section 4.3.2). The questions will cover the general characteristics and structure of CMOs, as well as the types of risk.

For further explanation, contact David Uthe at (301) 590-6695.

Correction to *Notice to Members 93-12* (February 1993)

Due to an editing error, footnote 7 on page 54 of *Notice to Members 93-12* (February 1993), "Questions and Answers About New NASD Rules Governing Investment Company Sales Charges — Article III, Sections 26(b) and (d) of the Rules of Fair Practice," is incorrect. The correct footnote language is:

⁷The SEC has stated that "[w]hether particular shareholder or other services are 'primarily intended to result in the sale of fund shares' and, therefore, must be paid under a 12b-1 plan, will depend on the surrounding circumstances." Investment Company Act Release No. 1643 (June 13, 1985).

SPECIAL NASD NOTICE TO MEMBERS 93-23

SEC Approves New NASD Margin Rules

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On February 24, 1993, the Securities and Exchange Commission (SEC) approved the NASD's new margin rules. The rules conform the NASD's margin rules to those of the New York Stock Exchange (NYSE) by replacing the current provisions of Article III, Section 30, Appendix A of the Rules of Fair Practice with rule language substantially identical to the NYSE margin rules. The rules also specify that they do not apply to any member designated to an examining authority other than the NASD pursuant to SEC Rule 17d-2. The new rules take effect April 19, 1993. The text of the new rules follows this Notice.

Background

On February 24, 1993, the Securities and Exchange Commission (SEC) approved the NASD's new margin rules. The rules conform the NASD's margin rules to those of the New York Stock Exchange (NYSE) by replacing the current provisions of Article III, Appendix A with rule language substantially identical to the NYSE margin rules.

Currently, Sections 2 and 4 of Appendix A provide for initial and minimum margin to be deposited and maintained under rules and formulas that differ from those of the NYSE in several respects. Under current Section 4, members need not evaluate the credit of customers nor establish higher margin requirements for securities or customers based on such evaluation; nor does it provide an option for members to take charges to their net capital in certain instances when good-faith credit has been extended. In addition, current Section 4 permits lower margins on U.S.

Government securities. Finally, under Section 4 members cannot establish "nonpurpose credit" accounts for customers, and the Section does not establish margin requirements for shelf-registered, control, and restricted securities or for "day traders." The new provisions resolve these differences by conforming the NASD's margin rules to those of the NYSE.

Description of Rule Change

Section 1 — New Section 1 of Appendix A exempts NASD members designated to another self-regulatory organization (SRO) for oversight of the member's compliance with applicable securities laws, rules, and regulations, and SRO rules under SEC Rule 17d-2 from the provisions of the rule. The current provisions of Section 1 of Appendix A exempt members of any other national securities exchange. The amendment to Section 1 will permit the designated examining authority to apply its own margin rules rather than the rules of another SRO, significantly simplifying examinations.

Section 2 — New Section 2 consists of definitions covering options transactions that are substantially the same as the definitions in NYSE Rule 700. The definitions apply to the margin requirements for options transactions set forth in Subsection 3(f)(2) of the NASD rule. NYSE Rule 431(f)(2), which is the NYSE's options margin rules, references the definitions in NYSE Rule 700, which is part of the NYSE's general options rules. There are no comparable definitions in current Section 4. Note that Subsection 3(b) will replace current Section 2 relating to initial margin requirements.

Section 3 — Unless stated below,

the language of the new Section 3 is the same as NYSE Rule 431 in all material respects. Subsection 3(f)(1) replaces current Section 3 for valuation of securities; however, the provision in current Section 3 permitting the NASD to require additional margin in the event of undue concentration remains intact. The following describes the provisions of new Section 3, and, where applicable, those current provisions of Schedule A that will be replaced:

Subsection 3(a) — Subsections 3(a)(1) through (8) are definitions of general applicability to the new margin rule. There are no comparable definitions in current Section 4.

Subsections 3(b) and 3(c) — New Subsections 3(b) and 3(c) establish initial and maintenance margin requirements and replace Section 2, Subsections 4(a)(1) through (3), and 4(a)(5) of current Appendix A. New Subsection 3(c)(5) establishes margins for American Stock Exchange Emerging Company Marketplace securities as approved by the SEC May 14, 1992 (rule filing SR-NASD-92-10).

Subsection 3(d) — New Subsection 3(d) requires members to establish procedures for evaluating customer credit and imposing higher margin than required by the other provisions of Section 3. Current Subsection 4(b)(3) permits the NASD to require 100 percent margin for certain securities in certain circumstances; otherwise, there is no comparable provision in Section 4.

Subsection 3(e)(1) — New Subsection 3(e)(1) sets margins at 10 percent of the current market value for convertible securities that are carried long and are offset against a short position in the resulting security, and 5 percent of the current market value for long

securities when the same security is carried long and short in the same account. Current Subsections 4(b)(1) and (2) require 10 percent in each case.

Subsection 3(e)(2)(A) — New Subsection 3(e)(2)(A) requires margins on obligations of the United States, ranging from 1 percent to 6 percent, based on times to maturity ranging from less than 1 year to 20 years or more, respectively. Current Subsection 4(a)(8)(i) imposes margins ranging from 1/2 percent to 3 percent for maturities of less than 1 year up to 10 years, respectively, and current Subsection 4(a)(7) requires margin at 5 percent for maturities greater than 10 years.

Subsection 3(e)(2)(B) — New Subsection 3(e)(2)(B) sets margins for “all other exempted securities” other than obligations of the United States at the greater of 15 percent of the current market value or 7 percent of the principal amount of the obligation. Current Subsection 4(a)(6) requires 25 and 15 respectively, whichever is lower.

Subsection 3(e)(2)(C) — New Subsection 3(e)(2)(C) sets margins for “non-convertible corporate debt securities” at the greater of 20 percent of the current market value or 7 percent of the principal amount, except for certain mortgage-related securities for which the margin is 5 percent of the current market value. There is no comparable provision in Section 4 currently; however, Subsection 4(a) requires margin of 25 percent of the market value of all securities long in the account, and Subsection 4(a)(8)(ii) permits the NASD to establish lower requirements on application.

Subsection 3(e)(2)(D) — New Subsection 3(e)(2)(D) permits members to clear and carry “basket transactions” for market makers at

margin rates satisfactory to the parties, provided the margin is adequate to cover all real and potential risks. This Subsection also permits the carrying member the option of taking a charge to net worth when computing net capital for any margin deficiency in the account, rather than requiring margin from the market maker. This provision differs slightly from the NYSE rule because the NYSE requires the computation of net capital under its Rule 325, while the NASD’s rule specifies the computation of net capital under SEC Rule 15c3-1. This provision replaces current Section 12.

Subsection 3(e)(2)(E)(i) — New Subsection 3(e)(2)(E)(i) permits members to offset maintenance margin requirements with accrued interest. This provision replaces current Section 15, which permits members to use only interest in government securities as an offset.

Subsection 3(e)(2)(E)(ii) — New Subsection 3(e)(2)(E)(ii) provides that the NASD may permit lower margin requirements on written application. This provision replaces current Subsection 4(a)(8)(ii).

Subsection 3(e)(2)(F) — New Subsection 3(e)(2)(F) provides that in cash transactions with customers involving issued exempted securities in a cash account, full payment must be made promptly; otherwise, a deposit shall be required as if it were a margin transaction. Transactions with members or non-member broker/dealers in issued exempted securities, however, do not require margin. This provision replaces current Subsection 6(a).

Subsection 3(e)(3) — New Subsection 3(e)(3) permits accounts in which a partner or stockholder of the carrying organization has an interest to maintain margin accord-

ing to Section 3 for all other participants in the account as if the partner's or stockholder's interest was in a separate account. There is no comparable provision in current Appendix A.

Subsection 3(e)(4) — New Subsection 3(e)(4) exempts international arbitrage accounts of non-member foreign broker/dealers from Appendix A; however, any deficiency between equity and required margin under Appendix A must be charged against the member's net capital. There is no comparable provision in current Appendix A.

Subsection 3(e)(5) — New Subsection 3(e)(5) permits a member to carry the account of a market maker on the margin provided for under the rule, *or*, as an option, on a margin basis satisfactory to both parties, *provided* the carrying member takes a deduction against net capital for any deficit below the required margin. This provision, along with Subsection 3(e)(2)(D) and 3(e)(6), replaces current Section 12.

Subsection 3(e)(6) — New Subsection 3(e)(6) permits a member to carry the proprietary account of another broker/dealer on margin satisfactory to the parties that complies with Federal Reserve Board Regulation T. The provision also permits the carrying member to take a deduction against net capital rather than require margin from the broker/dealer, provided the account is not in deficit equity condition. This provision, along with new Subsection 3(e)(2)(D) and 3(e)(5), replaces current Section 12.

Subsection 3(e)(7) — New Subsection 3(e)(7) permits members to establish "nonpurpose credit" accounts for customers. The term "nonpurpose credit" is defined

by reference to Section 220.2(u) of Regulation T. There is no comparable provision in current Appendix A.

Subsection 3(e)(8) — New Subsection 3(e)(8) establishes margin requirements for "shelf-registered," "control" and "restricted" securities. There is no comparable provision in current Appendix A.

Subsection 3(f)(1) — New Subsection 3(f)(1) provides that active securities are to be valued at current market prices, and other securities are to be valued after considering liquidation value, price volatility, and market liquidity. This provision replaces current Section 3.

Subsections 3(f)(2)(D)(i) through 3(f)(2)(K) — New Subsections 3(f)(2)(D)(i) through 3(f)(2)(K) establish margin requirements for options. These provisions typically require margin in excess of 100 percent of the current market value of any short option. These provisions replace current Subsections 4(a)(4), 4(a)(8)(i) through (vi), and Section 7.

Subsection 3(f)(3) — New Subsection 3(f)(3) provides that the margin required for securities "when issued" is the same as if the securities were issued. This provision replaces current Section 5.

Subsections 3(f)(4) and 3(f)(5) — New Subsections 3(f)(4) and 3(f)(5) permit the consolidation of any guaranteed account with another account, or the consolidation of any two accounts of a customer, for margin purposes, provided the guarantee or consolidation is agreed to in writing. These provisions replace current Sections 8 and 9.

Subsections 3(f)(6) and 3(f)(7) — Subsections 3(f)(6) and 3(f)(7) provide that members should collect required margin as quickly as possible and not permit customers routinely to meet Regulation T margin calls through the liquidation of account positions. These provisions replace current Sections 10 and 13.

Subsection 3(f)(8) — New Subsection 3(f)(8)(A) provides that the NASD may establish higher margin requirements than otherwise required by new Section 3. Current Subsection 4(b)(3) is comparable to this provision. New Subsection 3(f)(8)(B), for which there is no comparable provision in the current rule, establishes margin requirements for "day traders" and is consistent with the NYSE's margin rule.

Subsection 3(f)(9) — New Subsection 3(f)(9) provides that members may not permit customers to "free ride" by effecting transactions in cash accounts where the cost of the security is met by the sale of the same securities. There is no comparable provision in current Section 4.

Other changes — Current Sections 11 and 14, relating to recordkeeping requirements and the definition of "margin account," respectively, are being eliminated as redundant. Recordkeeping requirements are adequately covered by the current SEC rules, and the new NASD rules adequately define the terms necessary for interpretation of the rule.

The new rules are effective on April 19, 1993. Questions concerning this Notice may be directed to Walter J. Robertson, Director, Compliance Department at (202) 728-8236, or Derrick Black at (202) 728-8225.

Text of Appendix A to Article III, Section 30 of the Rules of Fair Practice

Sec. 1.

Exception

Any member designated to another self-regulatory organization for oversight of the member's compliance with applicable securities laws, rules and regulations, and self-regulatory organization rules under Securities and Exchange Commission Rule 17d-2 is exempt from the provisions of this Appendix.

Sec. 2.

Definitions Related to Options Transactions

The following definitions shall apply to options transactions:

(1) **Aggregate Discount Amount** — The term "aggregate discount amount" as used with reference to a Treasury bill option contract means the principal amount of the underlying Treasury bill (i) multiplied by the annualized discount (i.e., 100 percent minus the exercise price of the option contract) and (ii) further multiplied by a fraction having a numerator equal to the number of days to maturity of the underlying Treasury bill on the earliest date on which it could be delivered pursuant to the rules of the Options Clearing Corporation in connection with the exercise of the option (normally 91 or 182 days) and a denominator of 360.

(2) **Aggregate Exercise Price** — The term "aggregate exercise price" as used with reference to an option contract means:

(i) if a single stock underlies the option contract, the exercise price

of the option contract multiplied by the number of shares of the underlying stock covered by such option contract,

ii) if a Treasury bond or Treasury note underlies the option contract,

(A) the exercise price of the option contract multiplied by the principal amount of the underlying security covered by such option contract, plus (B) accrued interest:

(1) on bonds (except bonds issued or guaranteed by the United States Government), that portion of the interest on the bonds for a full year, computed for the number of days elapsed since the previous interest date on the basis of a 360-day-year. Each calendar month shall be considered to be 1/12 of 360 days, or 30 days, and each period from a date in one month to the same date in the following month shall be considered to be 30 days.

(2) on bonds issued or guaranteed by the United States Government, that portion of the interest on the bonds for the current full interest period, computed for the actual number of days elapsed since the previous interest date on the basis of actual number of calendar days in the current full interest period. The actual elapsed days in each calendar month shall be used in determining the number of days in a period.

Computation of elapsed days. — The following tables are given to illustrate the method of computing the number of elapsed days in conformity with the above section:

On bonds (except bonds issued or guaranteed by the United States Government):

• From 1st to 30th of the same month to be figured as 29 days

• From 1st to 31st of the same month to be figured as 30 days

• From 1st to 1st of the following month to be figured as 30 days.

Where interest is payable on 30th or 31st of the month:

• From 30th or 31st to 1st of the following month to be figured as 1 day

• From 30th or 31st to 30th of the following month to be figured as 30 days

• From 30th or 31st to 31st of the following month to be figured as 30 days

• From 30th or 31st to 1st of second following month, figured as 1 month, 1 day

On bonds issued or guaranteed by the United States Government:

• From 15th of a 28-day month to the 15th of the following month is 28 days

• From 15th of a 30-day month to the 15th of the following month is 30 days

• From 15th of a 31-day month to the 15th of the following month is 31 days.

The six month's interest period ending:

- January 15 is 184 days
- February 15 is 184 days
- March 15 is 181* days
- April 15 is 182* days
- May 15 is 181* days
- June 15 is 182* days
- July 15 is 181* days
- August 15 is 181* days
- September 15 is 184 days
- October 15 is 183 days
- November 15 is 184 days

- December 15 is 183 days

* Leap Year adds 1 day to this period.

(iii) if a Treasury bill underlies the option contract, the difference between the principal amount of such Treasury bill and the aggregate discount amount;

(iv) if an index stock group underlies the option contract, the exercise price of the option contract times the index multiplier; or

(v) if a GNMA underlies the option contract, the exercise price of the option contract multiplied by the nominal principal amount of the underlying GNMA covered by such option contract.

In the case of an underlying GNMA, if the remaining unpaid principal balance of a GNMA delivered upon exercise of an option contract is a permissible variant of, rather than equal to, the nominal principal amount, the aggregate exercise price shall be adjusted to equal the product of the exercise price and such remaining unpaid principal balance, plus in each case the appropriate differential.

(3) Annualized Discount — The term “annualized discount” as used with reference to a Treasury bill means the percent discount from principal amount at which the Treasury bill may be purchased or sold, expressed as a discount for a term to maturity of 360 days.

(4) Applicable Current Options Disclosure Document — The term “applicable current Options Disclosure Document” means, as to any kind of option, the most recent edition of the Options Disclosure Document and any supplement that pertains to that kind of option and that meets the requirements of Rule

9b-1 under the Securities Exchange Act of 1934, as amended.

(5) Appropriate Differential — The term “appropriate differential” as used with reference to a GNMA option contract means a positive or negative amount equal to the product of (i) the difference between the remaining unpaid principal balance of a GNMA delivered upon exercise of that contract and the nominal principal amount, and (ii) the difference between the current cash market price of GNMA's bearing the same stated rate of interest as that borne by the GNMA delivered upon exercise and the exercise price.

(6) Broad Index Stock Group — The term “broad index stock group” means an index stock group of 25 or more stocks whose inclusion and relative representation in the group are determined by the inclusion and relative representation of their current market prices in a widely-disseminated stock index reflecting the stock market as a whole or an inter-industry sector of the stock market.

(7) Broad Index Stock Group Option (Contract) — The term “broad index stock group option (contract)” means an option contract on a broad index stock group.

(8) Call — The term “call” means an option contract under which the holder has the right, in accordance with the terms of the option, to purchase from The Options Clearing Corporation:

- (i) the number of shares of the underlying stock (if a single stock underlies the option contract);
- (ii) the principal amount of the underlying security (if a Government security underlies the option contract);

(iii) the multiple of the current index group value of the underlying group (if an index stock group underlies the option contract); or

(iv) the nominal principal amount or any permissible variant of the underlying GNMA (if a GNMA underlies the option contract) covered by the option contract.

(9) Class (of Options) — The term “class (of options)” means all option contracts of the same type and kind covering the same underlying security or underlying stock group.

(10) Clearing Member — The term “clearing member” means a member which has been admitted to membership in The Options Clearing Corporation pursuant to the provisions of the rules of The Options Clearing Corporation.

(11) Closing Purchase Transaction — The term “closing purchase transaction” means an option transaction in which the purchaser’s intention is to reduce or eliminate a short position in the series of options involved in such transaction.

(12) Closing Sale Transaction — The term “closing sale transaction” means an option transaction in which the seller’s intention is to reduce or eliminate a long position in the series of options involved in such transaction.

(13) Complement — The term “complement,” as used with reference to an annualized discount, means the difference between 100 percent and the annualized discount.

(14) Covered

(i) The term “covered” in respect of a short position in a call option

contract means that the writer's obligation is secured either by a "specific deposit" or an "escrow deposit" meeting the conditions of Rule 610(e) or 610(h), respectively, of the rules of The Options Clearing Corporation, or by a letter of guarantee meeting the requirements of Section 3(f)(2)(H)(iv) of the appendix or that the writer holds in the same account as the short position,

(A) on a share-for-share basis (if a single stock underlies the option contract),

(B) on the basis of a matching principal amount (if a Government security underlies the option contract),

(C) on the basis of market value ("covering" underlying stocks) or of the index multiplier ("covering" option contracts) (if an index stock group underlies the option contract), or

(D) on the basis of the remaining unpaid principal balance (if a GNMA underlies the option contract),

a long position either in the underlying security or underlying index stock group or in an option contract of the same class having an expiration date on or subsequent to the expiration date of the option contract in such short position and having an exercise price equal to or less than the exercise price of the option contract in such short position.

(ii) The term "covered" in respect of a short position in a put option contract means that the writer's obligation is secured by a letter of guarantee meeting the requirements of Section 3(f)(2)(H)(iv) of this appendix or that the writer holds in the same account as the

short position,

(A) on a share-for-share basis (if a single stock underlies the option contract),

(B) on the basis of a matching principal amount (if a Government security underlies the option contract),

(C) on the basis of the index multiplier (if an index stock group underlies the option contract), or

(D) on the basis of a matching remaining unpaid principal balance (if a GNMA underlies the option contract),

a long position in an option contract of the same class having an expiration date on or subsequent to the expiration date of the option contract in such short position and having an exercise price equal to or greater than the exercise price of the option contract in such short position.

(iii) In the case of a "covering" underlying GNMA, the remaining unpaid principal balance must equal to or be a permissible variant of, the nominal principal amount and the "covering" underlying GNMA must bear a qualifying rate of interest.

(15) Current Cash Market Price — The term "current cash market price" as used with reference to GNMA means the prevailing price in the cash market for GNMA bearing a particular stated rate of interest to be delivered on the next applicable monthly settlement date determined in the manner specified in the rules of The Options Clearing Corporation.

(16) Current Options Disclosure Document — See "Applicable Current Options Disclosure Document."

(17) Current Index Group Value — The term "current index group value" means \$1.00 multiplied by the current value reported for the index that is derived from the current market prices of the stocks in the group. When used with reference to the exercise of an index stock group option, the value is the last one reported on the day of exercise or, if the day of exercise is not a trading day, on the last trading day before exercise.

(18) Designated Rate — The term "designated rate" as used with reference to a GNMA option means a rate of interest of eight percent or such other rate as may be designated in the manner specified in the rules of The Options Clearing Corporation.

(19) Dominant Underlying Stock — The term "dominant underlying stock" means, when used with reference to an industry index stock group, a stock that accounts for 30 percent or more of the index group value.

(20) Exchange Option Transaction — The term "Exchange option transaction" means an option transaction effected on the floor of a registered securities exchange between or among members.

(21) Exchange Options Trading — The term "Exchange options trading" means options trading on the floor of a registered securities exchange.

(22) Exercise Price — The term "exercise price" in respect of an option contract means:

(i) if a single stock underlies the option contract, the stated price per share at which the underlying stock;

(ii) if a Treasury bond or Treasury note underlies the option contract,

the specified percentage of the principal amount at which the underlying Treasury security;

(iii) if a Treasury bill underlies the option contract, the specified complement of the annualized discount at which the underlying Treasury bill;

(iv) if an index stock group underlies the option contract, the specified index group value at which the current index group value; or

(v) if a GNMA underlies the option contract, the specified percentage of the nominal principal amount (assuming delivery of a GNMA bearing a stated rate of interest equal to the designated rate at which the underlying GNMA) may be purchased (in the case of a call) or sold (in the case of a put) upon the exercise of such option contract. In the case of an underlying GNMA, if the stated rate of interest of a GNMA delivered upon exercise of an option contract is a qualifying rate other than the designated rate, the exercise price shall be an amount which provides the same yield to maturity as the amount which would have been payable if the stated rate of interest had been equal to the designated rate (assuming a 30-year term and prepayment at the end of the twelfth year of the mortgage obligations underlying GNMA).

(23) Expiration Date — The term “expiration date” in respect of an option contract means the date and time fixed by the rules of The Options Clearing Corporation for the expiration of all option contracts covering the same underlying security or underlying index stock group and having the same expiration month as such option contract.

(24) Expiration Month — The term “expiration month” in respect of an

option contract means the month and year in which such option contract expires.

(25) GNMA — The term “GNMA” means a mortgage pass-through security guaranteed as to timely payment of principal and interest by the Government National Mortgage Association, as described in the current standard prospectus of the Department of Housing and Urban Development covering such securities, bearing a stated rate of interest which is a qualifying rate. Any two or more separate certificates representing GNMA's bearing the same qualifying rate delivered in accordance with the rules of The Options Clearing Corporation upon exercise of an option contract shall, for purposes of this Section, be deemed to be a single GNMA, having a remaining unpaid principal balance equal to the sum of the remaining unpaid principal balances of such separate certificates.

(26) GNMA Option (Contract) — The term “GNMA option (contract)” means an option contract on GNMA's.

(27) GNMA Production Rate — The term “GNMA production rate” means a rate of interest .50 percent below the maximum stated rate of interest on residential mortgages which the Federal Housing Administration is willing to insure and which the Veterans Administration is willing to guarantee, as it may vary from time to time in accordance with official announcements of changes in such rates made by the Federal Housing Administration.

(28) Government Security — The term “Government security” means a bond, note, bill, debenture or other evidence of indebtedness that is a direct obligation of, or an obligation guaranteed as to principal or

interest by, the United States or a corporation in which the United States has a direct or indirect interest (except debt securities guaranteed as to timely payment of principal and interest by the Government National Mortgage Association).

(29) Government Security Option (Contract) — The term “Government security option (contract)” means an option contract on Government securities.

(30) Index Multiplier — The term “index multiplier” as used with reference to an index stock group option contract means the amount specified in the contract by which the current index group value is to be multiplied to arrive at the value required to be delivered to the holder of a call or by the holder of a put upon valid exercise of the contract.

(31) Index Stock Group — The term “index stock group” means either a broad index stock group or an industry index stock group.

(32) Index Stock Group Option (Contract) — The term “index stock group option (contract)” means either a broad index stock group option contract or an industry index stock group option contract.

(33) Industry Index Stock Group — The term “industry index stock group” means an index stock group of six or more stocks whose inclusion and relative representation in the group are determined by the inclusion and relative representation of their current market prices in a widely-disseminated stock index reflecting a particular industry or closely-related industries.

(34) Industry Index Stock Group Option (Contract) — The term “industry index stock group option (contract)” means an option con-

tract on an industry index stock group.

(35) Kind of Option — The term “kind of option” means either a stock option contract, a Government security option contract, a broad index stock group option contract, an industry index stock group option contract or a GNMA option contract.

(36) Long Position — The term “long position” means the number of outstanding option contracts of a given series of options held by a person (purchaser).

(37) Nominal Principal Amount — The term “nominal principal amount” as used with reference to a GNMA option means the remaining unpaid principal balance of GNMA required to be delivered to the holder of a call or by the holder of a put upon exercise of an option without regard to any variance in the remaining unpaid principal balance permitted to be delivered upon such exercise and shall be \$100,000 in the case of a single call or put.

(38) Opening Purchase Transaction — The term “opening purchase transaction” means an option transaction in which the purchaser’s intention is to create or increase a long position in the series of options involved in such transaction.

(39) Opening Writing Transaction — The term “opening writing transaction” means an option transaction in which the seller’s (writer’s) intention is to create or increase a short position in the series of options involved in such transaction.

(40) Option (Contract) — The term “option (contract)” means a put or a call issued, or subject to issuance, by The Options Clearing

Corporation pursuant to the rules of The Options Clearing Corporation.

(41) Option Transaction — The term “option transaction” means a transaction for the purchase or sale of an option contract, or for the closing out of a long or short position in an option contract.

(42) Options Trading — The term “options trading” means trading in any option issued by The Options Clearing Corporation, whether or not of a type, class or series which has been approved for trading on Nasdaq or on a national securities exchange.

(43) Outstanding — The term “outstanding” in respect of an option contract means an option contract which has been issued by The Options Clearing Corporation and has neither been the subject of a closing sale transaction on or through the facilities of, or otherwise subject to the rules of, a Participating Exchange or Association nor been exercised nor reached its expiration date.

(44) Participating Exchange (Association) — The term “Participating Exchange (Association)” means a national securities exchange (association) which has qualified for participation in The Options Clearing Corporation.

(45) Primary Market — The term “primary market” means (i) in respect of an underlying security that is principally traded on a national securities exchange, the principal exchange market in which the underlying security is traded and (ii) in respect of an underlying security that is principally traded in the over-the-counter market, the market reflected by any widely recognized quotation dissemination system or service (The National

Association of Securities Dealers, Inc. Automated Quotation System (“NASDAQ”) in the case of a NASDAQ stock).

(46) Public Customer of a Member Organization — The term “public customer of a member organization” means a customer that is not a broker or a dealer.

(47) Put — The term “put” means an option contract under which the holder has the right, in accordance with the terms of the option, to sell to The Options Clearing Corporation:

(i) the number of shares of the underlying stock (if a single stock underlies the option contract);

(ii) the principal amount of the underlying security (if a Government security underlies the option contract);

(iii) the multiple of the current index group value of the underlying group (if an index stock group underlies the option contract); or

(iv) the nominal principal amount or any permissible variant of the underlying GNMA (if a GNMA underlies the option contract) covered by the option contract.

(48) Qualifying Rate — The term “qualifying rate” as used with reference to a GNMA option means any rate of interest equal to or less than the GNMA production rate; provided that:

(i) in the event of any increase in the GNMA production rate, a GNMA issued prior to the date of any such change bearing a stated rate of interest equal to any such increased GNMA production rate (or any lower rate of interest which was not a qualifying rate on the day prior to that date) shall be deemed

not to bear a qualifying rate until the expiration of 45 days from the date of such increase or until after the settlement date for options on GNMA's following the next expiration date for any series of such options, whichever shall last occur unless such GNMA bears a stated rate of interest deemed to constitute a qualifying rate in accordance with subparagraph (ii) below; and

(ii) in the event of any decrease in the GNMA production rate, a GNMA bearing a stated rate of interest which was equal to the GNMA production rate (or any lower rate of interest which is not otherwise a qualifying rate) on the day prior to the date of any such decrease shall be deemed to continue to bear a qualifying rate for a period of 45 days from the date of such decrease or until the settlement date for options on GNMA's following the next expiration date for any series of such options, whichever shall last occur.

(49) Registered Clearing Agency — The term “registered clearing agency” shall mean a clearing agency as defined in Section (3)(a)(23) of the Securities Exchange Act of 1934 that is registered with the Securities and Exchange Commission pursuant to Section 17A(b)(2) of the Act.

(50) Registered Options Principal — The term “Registered Options Principal” means a person who has qualified as a “Registered Options Principal.”

(51) Registered Options Representative — The term “Registered Options Representative” means a registered representative who has qualified as a “Registered Options Representative.”

(52) Related Security — The term

“related security” means:

(i) as used with reference to a Government security option, (A) all securities underlying Government security options, (B) futures contracts on such underlying security and (C) all options on such futures contracts;

(ii) as used with reference to a stock option, the underlying stock; and

(iii) as used with reference to an index stock group options, (A) all futures contracts on the underlying stock group or on any substantially identical index stock group, all options contracts on any substantially identical index stock group, and all options on such futures contracts and (B) also, in the case of an industry index stock group option only, all underlying stocks accounting for five percent or more of the current index group value of the underlying industry index stock group and all individual stock options on such underlying stocks.

(53) Rules of The Options Clearing Corporation — The term “rules of The Options Clearing Corporation” means the by-laws and the rules of The Options Clearing Corporation and all written interpretations thereof, as the same may be in effect from time to time.

(54) Series (of Options) — The term “series (of options)” means all option contracts of the same class of options having the same expiration date, exercise price and unit of trading.

(55) Shares — The term “shares” means the basic unit of issue of a stock.

(56) Short Position — The term “short position” means the number of outstanding option contracts of a given series of options with respect

to which a person is obligated as a writer (seller).

(57) Stock — The term “stock” shall be broadly interpreted to mean any equity security, as defined in Section 3(a)(11) of the Securities Exchange Act of 1934, as amended, and Rule 3a11-1 under the Act, that confers directly on the holder a present equity ownership or participation interest in an enterprise.

(58) Stock Option (Contract) — The term “stock option (contract)” means an option contract on a single stock.

(59) Stock-Related Option (Contract) — The term “stock-related option (contract)” means either a stock option contract, a broad industry index stock group option contract or any industry index stock group option contract.

(60) The Options Clearing Corporation — The term “The Options Clearing Corporation” means The Options Clearing Corporation, a subsidiary of the Participating Exchanges and Association.

(61) Treasury Bill — The term “Treasury bill” means a Government security sold by the U.S. Treasury Department at a discount from principal amount, bearing no interest and normally having a term to maturity of not more than one year at the time of original issue.

(62) Treasury Bond — The term “Treasury bond” means a Government security sold by the U.S. Treasury that has been designated by the U.S. Treasury Department with reference to its term to maturity as a “bond” (normally confined to Treasury securities with a term to maturity of more than ten years at the time of original issue).

(63) Treasury Note — The term “Treasury note” means a Government security sold by the U.S. Treasury Department that has been designated by the U.S. Treasury Department with reference to its term to maturity as a “note” (normally confined to Treasury securities with a term to maturity of more than one year but not more than ten years at the time of original issue).

(64) Type of Option — The term “type of option” means the classification of an option contract as either a put or a call.

(65) Uncovered — The term “uncovered” in respect of a short position in an option contract means that the short position is not covered.

(66) Underlying Government Security — The term “underlying Government security” means an underlying security that is a Government security.

(67) Underlying GNMA — The term “underlying GNMA” means an underlying security that is a GNMA.

(68) Underlying (Index) Stock Group — The term “underlying (index) stock group” as used with reference to an index stock group option contract means the index stock group, a multiple of the current index group value of which The Options Clearing Corporation is obligated to sell (in the case of a call) or purchase (in the case of a put) upon valid exercise of the contract.

(69) Underlying Security — The term “underlying security” means:

(i) as used with reference to an option contract other than an index stock group option contract, the

security which The Options Clearing Corporation is obligated to sell (in the case of a call) or purchase (in the case of a put) upon valid exercise of the contract; and

(ii) as used with reference to an index stock group option contract, any of the stocks included in the underlying index stock group.

(70) Underlying Stock — The term “underlying stock” means an underlying security that is a stock.

Sec. 3.

Margin Requirements

Definitions

(a) For purposes of this Section, the following terms shall have the meanings specified below:

(1) The term “current market value” means the total cost or net proceeds of a security on the day it was purchased or sold or at any other time the preceding business day’s closing price as shown by any regularly published reporting or quotation service. If there is no closing price, a member organization may use a reasonable estimate of the market value of the security as of the close of business on the preceding business day.

(2) The term “customer” means any person for whom securities are purchased or sold or to whom securities are purchased or sold whether on a regular way, when issued, delayed or future delivery basis. It will also include any person for whom securities are held or carried and to or for whom a member organization extends, arranges or maintains any credit. The term will not include a broker or dealer from whom a security has been purchased or to whom a security has been sold for the account of the

member organization or its customers.

(3) The term “designated account” means the account of a bank, trust company, insurance company, investment trust, state or political subdivision thereof, charitable or nonprofit educational institution regulated under the laws of the United States or any state, or pension or profit sharing plan subject to ERISA or of any agency of the United States or of a state or a political subdivision thereof.

(4) The term “equity” means the customer’s ownership interest in the account, computed by adding the current market value of all securities “long” and the amount of any credit balance and subtracting the current market value of all securities “short” and the amount of any debit balance.

(5) The term “exempted security” or “exempted securities” has the meaning as in Section 3(a)(12) of the Securities Exchange Act of 1934.

(6) The term “margin” means the amount of equity to be maintained on a security position held or carried in an account.

(7) The term “person” has the meaning as in Section 3(a)(9) of the Securities Exchange Act of 1934.

(8) The term “basket” shall mean a group of stocks that the Association or any national securities exchange designates as eligible for execution in a single trade through its trading facilities and that consists of stocks whose inclusion and relative representation in the group are determined by the inclusion and relative representation of their current market prices in a widely-disseminated stock index reflecting the stock market as a whole.

Initial margin

(b) For the purpose of effecting new securities transactions and commitments, the customer shall be required to deposit margin in cash and/or securities in the account which shall be at least the greater of:

(1) the amount specified in Regulation T of the Board of Governors of the Federal Reserve System; or

(2) the amount specified in section (c) of this Section; or

(3) such greater amount as the Association may from time to time require for specific securities; or

(4) equity of at least \$2,000 except that cash need not be deposited in excess of the cost of any security purchased (this equity and cost of purchase provision shall not apply to “when distributed” securities in a cash account).

Withdrawals of cash or securities may be made from any account which has a debit balance, “short” position or commitments, provided it is in compliance with Regulation T of the Board of Governors of the Federal Reserve System and after such withdrawal the equity in the account is at least the greater of \$2,000 or an amount sufficient to meet the maintenance margin requirements of this Section.

Maintenance margin

(c) The margin which must be maintained in margin accounts of customers shall be as follows:

(1) 25 percent of the current market value of all securities “long” in the account; plus

(2) \$2.50 per share or 100 percent

of the current market value, whichever amount is greater, of each stock “short” in the account selling at less than \$5.00 per share; plus

(3) \$5.00 per share or 30 percent of the current market value, whichever amount is greater, of each stock “short” in the account selling at \$5.00 per share or above; plus

(4) 5 percent of the principal amount or 30 percent of the current market value, whichever amount is greater, of each bond “short” in the account.

(5) In the case of securities listed on the Emerging Company Marketplace of the American Stock Exchange (AMEX), 100 percent of the market value in cash, of each security held “long” in the account, unless the AMEX determines that the security satisfies the criteria enumerated in Sections 220.17(a) and (b) of Regulation T of the Board of Governors of the Federal Reserve System for inclusion and continued inclusion on the List of OTC Margin Stocks, except for the requirement relating to the number of dealers in Sections 220.17(a)(1) and (b)(1).

Additional margin

(d) Procedures shall be established by members to:

(1) review limits and types of credit extended to all customers;

(2) formulate their own margin requirements; and

(3) review the need for instituting higher margin requirements, mark-to-markets and collateral deposits than are required by this Section for individual securities or customer accounts.

Exceptions to Section

(e) The foregoing requirements of this Section are subject to the following exceptions:

(1) Offsetting “Long” and “Short” Positions — When a security carried in a “long” position is exchangeable or convertible within a reasonable time, without restriction other than the payment of money, into a security carried in a “short” position for the same customer, the margin to be maintained on such positions shall be 10 percent of the current market value of the “long” securities. When the same security is carried “long” and “short” the margin to be maintained on such positions shall be 5 percent of the current market value of the “long” securities. In determining such margin requirements, “short” positions shall be marked to the market.

(2) Exempted Securities, Marginable Corporate Debt Securities and Baskets

(A) Obligations of the United States — On net “long” or net “short” positions in obligations (including zero coupon bonds, i.e., bonds with coupons detached or non-interest bearing bonds) issued or guaranteed as to principal or interest by the United States Government or issued or guaranteed by corporations in which the United States has a direct or indirect interest as shall be designated for exemption by the Secretary of the Treasury, the margin to be maintained shall be the percentage of the current market value of such obligations as specified in the applicable category below:

(i) Less than one year to maturity, 1 percent

(ii) One year but less than three years to maturity, 2 percent

(iii) Three years but less than five years to maturity, 3 percent

(iv) Five years but less than ten years to maturity, 4 percent

(v) Ten years but less than twenty years to maturity, 5 percent

(vi) Twenty years or more to maturity, 6 percent

Notwithstanding the above, on zero coupon bonds with five years or more to maturity the margin to be maintained shall not be less than 3 percent of the principal amount of the obligation.

When such obligations other than United States Treasury bills are due to mature in thirty calendar days or less, a member, at its discretion, may permit the customer to substitute another such obligation for the maturing obligation and use the margin held on the maturing obligation to reduce the margin required on the new obligation, provided the customer has given the member irrevocable instructions to redeem the maturing obligation.

(B) All Other Exempted Securities — On any positions in exempted securities other than obligations of the United States, the margin to be maintained shall be 15 percent of the current market value or 7 percent of the principal amount of such obligation, whichever amount is greater.

(C) Non-Convertible Corporate Debt Securities — On any positions in non-convertible corporate debt securities, which are listed or traded on a registered national securities exchange or qualify as an “OTC margin bond,” as defined in Section 220.2(t) of Regulation T of the Board of Governors of the Federal Reserve System, the margin to be maintained shall be 20 percent of

the current market value or 7 percent of the principal amount, whichever amount is greater, except on mortgage related securities as defined in Section 3(a)(41) of the Securities Exchange Act of 1934; the margin to be maintained for an exempt account shall be 5 percent of the current market value.

For purposes of this paragraph 3(e)(2)(C), an exempt account shall be defined as a member, non-member broker/dealer, “designated account” or any person having net tangible assets of at least sixteen million dollars.

(D) Baskets — Notwithstanding the other provisions of this Section, a member may clear and carry basket transactions of one or more members registered as market-makers (who are deemed specialists for purposes of Section 7 of the Securities Exchange Act of 1934 pursuant to the rules of a national securities exchange) upon a margin basis satisfactory to the concerned parties, provided all real and potential risks in accounts carried under such arrangements are at all times adequately covered by the margin maintained in the account or, in the absence thereof, by the carrying member when computing net capital under SEC Rule 15c3-1.

(E) Special Provisions — Notwithstanding the foregoing in this Subsection 3(e)(2);

(i) A member may, at its discretion, permit the use of accrued interest as an offset to the maintenance margin required to be maintained; and

(ii) The Association upon written application, may permit lower margin requirements on a case-by-case basis.

(F) Cash Transactions With Customers — When a customer

purchases an issued exempted security from or through a member in a cash account, full payment shall be made promptly. If, however, delivery or payment therefore is not made promptly after the trade date, a deposit shall be required as if it were a margin transaction, unless it is a transaction with a “designated account.”

On any position resulting from a transaction in issued exempted securities made for a member, or a non-member broker/dealer, or made for or with a “designated account,” no margin need be required and such position need not be marked to the market. However, where such position is not marked to the market, an amount equal to the loss at the market in such position shall be charged against the member’s net capital as provided in SEC Rule 15c3-1.

(3) Joint Accounts in Which the Carrying Organization or a Partner or Stockholder Therein Has an Interest — In the case of a joint account carried by a member in which such member, or any partner, or stockholder (other than a holder of freely transferable stock only) of such member participates with others, each participant other than the carrying member shall maintain an equity with respect to such interest pursuant to the margin provisions of the Section as if such interest were in a separate account.

The Association will consider requests for exemption from the provisions of this Subsection 3(e)(3), provided

(A) the account is confined exclusively to transactions and positions in exempted securities; or

(B) the account is maintained as a Market Functions Account conforming to the conditions of Section

220.12(e) (Odd-lot dealers) of Regulation T of the Board of Governors of the Federal Reserve System; or

(C) the account is maintained as a Market Functions Account conforming to the conditions of Section 220.12(c) (Underwritings and Distributions) of Regulation T of the Board of Governors of the Federal Reserve System

and each other participant margins his share of such account on such basis as the Association may prescribe.

(4) International Arbitrage Accounts — International arbitrage accounts for non-member foreign brokers or dealers who are members of a foreign securities exchange shall not be subject to this Section. The amount of any deficiency between the equity in such an account and the margin required by the other provisions of this Section shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(5) Specialists' and Market Makers' Accounts —

(A) A member may carry the account of an "approved specialist or market maker," which account is limited to specialist or market making transactions, upon a margin basis which is satisfactory to both parties. The amount of any deficiency between the equity in the account and the margin required by the other provisions of this Section shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

For the purpose of this paragraph 3(e)(5)(A), the term "approved specialist or market maker" means either:

(i) a specialist or market maker, who is deemed a specialist for all purposes under the Securities Exchange Act of 1934 and who is registered pursuant to the rules of a national securities exchange; or

(ii) an OTC market maker or third market maker, who meets the requirements of Section 220.12(d) of Regulation T of the Board of Governors of the Federal Reserve System.

(B) In the case of a joint account carried by a member in accordance with paragraph 3(e)(5)(A) above in which the member participates, the equity maintained in the account by the other participants may be in any amount which is mutually satisfactory. The amount of any deficiency between the equity maintained in the account by the other participants and their proportionate share of the margin required by the other provisions of this Section shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(6) Broker/Dealer Accounts — A member may carry the proprietary account of another broker/dealer, which is registered with the Securities and Exchange Commission, upon a margin basis which is satisfactory to both parties, provided the requirements of Regulation T of the Board of Governors of the Federal Reserve System are adhered to and the account is not carried in a deficit equity condition. The amount of any deficiency between the equity maintained in the account and the margin required by the other provisions of this Section shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(7) Nonpurpose Credit — In a non-securities credit account, a member

may extend and maintain nonpurpose credit to or for any customer without collateral or on any collateral whatever, provided:

(A) the account is recorded separately and confined to the transactions and relations specifically authorized by Regulation T of the Board of Governors of the Federal Reserve System;

(B) the account is not used in any way for the purpose of evading or circumventing any regulation of the Association or of the Board of Governors of the Federal Reserve System; and

(C) the amount of any deficiency between the equity in the account and the margin required by the other provisions of this Section shall be charged against the member's net capital as provided in SEC Rule 15c3-1.

The term "nonpurpose credit" means an extension of credit other than "purpose credit" as defined in Section 220.2(u) of Regulation T of the Board of Governors of the Federal Reserve System.

(8) Shelf-Registered, Control and Restricted Securities

(A) Shelf-Registered Securities — The equity to be maintained in margin accounts of customers for securities which are the subject of a current and effective registration for a delayed offering (shelf-registered securities) shall be at least the amount of margin required by Subsection 3(c) of this Section, provided the member:

(i) obtains a current prospectus in effect with the Securities and Exchange Commission, meeting the requirements of Section 10 of the Securities Act of 1933, covering such securities;

(ii) has no reason to believe the Registration Statement is not in effect or that the issuer has been delinquent in filing such periodic reports as may be required of it with the Securities and Exchange Commission and is satisfied that such registration will be kept in effect and that the prospectus will be maintained on a current basis; and

(iii) retains a copy of such Registration Statement, including the prospectus, in an easily accessible place in its files.

Shelf-registered securities which do not meet all the conditions prescribed above shall have no value for purposes of this Section. (Also see paragraph 3(e)(8)(C).)

(B) Control and Restricted Securities — The equity in accounts of customers for control securities and other restricted securities of issuers who continue to maintain a consistent history of filing annual and periodic reports in timely fashion pursuant to the formal continuous disclosure system under the Securities Exchange Act of 1934, which are subject to Rule

144 or 145(d) under the Securities Act of 1933, shall be 40 percent of the current market value of such securities “long” in the account, provided the member:

(i) in computing net capital, deducts any margin deficiencies in customers’ accounts based upon a margin requirement as specified in subparagraph 3(C)(ii) of this Subsection 3(e)(8) for such securities and values only that amount of such securities which are then saleable under Rule 144 or 145(d) under the Securities Act of 1933 in conformity with all of the applicable terms and conditions thereof, for purposes of determining such deficiencies; and

(ii) makes volume computations necessary to determine the amount of securities then saleable under Rule 144 or 145(d) under the Securities Act of 1933 on a weekly basis or at such frequency as the member and/or the Association may deem appropriate under the circumstances. (Also see paragraph 3(e)(8)(C).)

(C) Additional Requirements on Shelf-Registered Securities and Control and Restricted Securities — A member extending credit on shelf-registered, control and other restricted securities in margin accounts of customers shall be subject to the following additional requirements:

(i) The Association may at any time require reports from members showing relevant information as to the amount of credit extended on shelf-registered, control and restricted securities and the amount, if any, deducted from net capital due to such security positions.

(ii) **Concentration Reduction** — A concentration exists whenever the aggregate position in control and restricted securities of any one issue exceeds (1) 10 percent of the outstanding shares or (2) 100 percent of the average weekly volume during the preceding three-month period. Where a concentration exists, for purposes of computing subparagraph (B)(i) of this Subsection 3(e)(8), the margin requirement on such securities shall be, based on the greater of (1) or (2) above, as specified below:

Percent of Outstanding Shares	Percent of Average Weekly Volume	Margin Requirement
• Up to 10 percent	• Up to 100 percent	• 25 percent
• Over 10 percent and under 15 percent	• Over 100 percent and under 200 percent	• 30 percent
• 15 percent and under 20 percent	• 200 percent and under 300 percent	• 45 percent
• 20 percent and under 25 percent	• 300 percent and under 400 percent	• 60 percent
• 25 percent and under 30 percent	• 400 percent and under 500 percent	• 75 percent
• 30 percent and above	• 500 percent and above	• 100 percent

(D) Restricted Securities — Securities either:

(i) held by non-affiliates of the issuer which are then saleable by the non-affiliate pursuant to the terms and conditions of Rule 144(k) under the Securities Act of 1933, or

(ii) which have been acquired by non-affiliates of the issuer in connection with a Rule 145(a) transaction under the Securities Act of 1933 which are then saleable by such non-affiliate pursuant to the terms and conditions of Rule 145(d)(2) or (d)(3) under such Act,

shall not be subject to the provisions of this Subsection 3(e)(8), provided that the issuer continues to maintain a consistent history of filing annual and periodic reports in timely fashion pursuant to the formal continuous disclosure system under the Securities Exchange Act of 1934.

Other Provisions

(f)(1) Determination of Value for Margin Purposes — Active securities dealt in on a national securities exchange or OTC marginable securities listed on Nasdaq shall, for margin purposes, be valued at current market prices. Other securities shall be valued conservatively in view of current market prices and the amount which might be realized upon liquidation. Sub-

stantial additional margin must be required in all cases where the securities carried in “long” or “short” positions are subject to unusually rapid or violent changes in value, or do not have an active market on Nasdaq or on a national securities exchange, or where the amount carried is such that the position(s) cannot be liquidated promptly.

(2) Puts, Calls and Other Options

(A) Except as provided below, no put or call carried for a customer shall be considered of any value for the purpose of computing the margin to be maintained in the account of such customer.

(B) The issuance, guarantee or sale (other than a “long” sale) for a customer of a put or a call shall be considered a security transaction subject to Section (b) of this Section.

(C) For purposes of this Subsection 3(f)(2), obligations issued by the United States Government shall be referred to as United States Government obligations. Mortgage pass-through obligations guaranteed as to timely payment of principal and interest by the Government National Mortgage Association shall be referred to as GNMA obligations. The terms “current market value” or “current market price” of an option shall mean the total cost or net proceeds of the option contract on the day the option was pur-

chased or sold and at any other time shall be the preceding business day’s closing price of that option (times the appropriate unit of trading or multiplier) as shown by any regularly published reporting or quotation service. The term “exercise settlement amount” shall mean the difference between the “aggregate exercise price” and the “aggregate current index value” (as such terms are defined in the pertinent By-Laws of the Options Clearing Corporation).

(D) The margin required on any put or call issued, guaranteed or carried “short” in a customer’s account shall be:

(i) In the case of puts and calls issued by a registered clearing agency, 100 percent of the current market value of the option plus the percentage of the current market value of the underlying security or index specified in column II of this paragraph (D)(i) below.

Notwithstanding the margin required below, the minimum margin on any put or call issued, guaranteed or carried “short” in a customer’s account may be reduced by any “out-of-the-money amount” (as defined in this paragraph (D)(i) below), but shall not be less than 100 percent of the current market value of the option plus the percentage of the current market value of the underlying security or index specified in column III of this paragraph (D)(i) below.

	I	II	III	IV
	Security or Index	Initial and/or Maintenance Margin Required	Minimum Margin Required	Underlying Component Value
(1)	Stock	20 percent	10 percent	The equivalent number of shares at current market prices
(2)	Industry index stock group	20 percent	10 percent	The product of the current index group value and the applicable index multiplier
(3)	Broad index stock group	15 percent	10 percent	The product of the current index group value and the applicable index multiplier
(4)	U.S. Treasury bills 95 days or less to maturity	.35 percent	1/20 percent	The underlying principal amount
(5)	U.S. Treasury notes	3 percent	1/2 percent	The underlying principal amount
(6)	U.S. Treasury bonds	3.5 percent	1/2 percent	The underlying principal amount
(7)	Foreign Currencies	4 percent	3/4 percent	The product of units per foreign currency contract and the closing spot price

For purposes of this subsection (D)(i), "out-of-the-money amounts" are determined as follows:

Option Issue	Call	Put
Stock Options	Any excess of the aggregate exercise price of the option over the current market value of the equivalent number of shares of the underlying security.	Any excess of the current market value of the equivalent number of shares of the underlying security over the aggregate exercise price of the option.
U.S. Treasury Options	Any excess of the aggregate exercise price of the option over the current market value of the underlying principal amount.	Any excess of the current market value of the underlying principal amount over the aggregate exercise price of the option.
Index Stock Group Options	Any excess of the aggregate exercise price of the option over the product of the current index group value and the applicable multiplier.	Any excess of the product of the current index group value and the applicable multiplier over the aggregate exercise price of the option.
Foreign Currency Options	Any excess of the aggregate exercise price of the option over the product of units per foreign currency contract and the closing spot prices.	The product of units per foreign currency contract and the closing spot prices over the aggregate price of the option.

If the option contract provides for the delivery of obligations with different maturity dates or coupon rates, the computation of the “out-of-the-money amount,” if any, where required by this Section, shall be made in such a manner as to result in the highest margin requirement on the short option position.

(ii) In the case of puts and calls issued by a registered clearing agency which represent options on GNMA obligations in the principal amount of \$100,000, 130 percent of the current market value of the option plus \$1,500, except that the margin required need not exceed \$5,000 plus the current market value of the option.

(iii) In the case of puts and calls not issued by a registered clearing agency and representing stock options or index stock group options, 100 percent of the option premium received plus 45 percent of the current market value of the equivalent number of shares of the underlying security or the product of the current index group value of the underlying index stock group and the applicable index multiplier, reduced by any excess of the exercise price over the current market value of the underlying security or the product of the current index group value of the underlying index stock group and the applicable multiplier, in the case of a call, or any excess of the current market value of the underlying security or the product of the current index group value of the underlying index stock group and the applicable multiplier, over the exercise price, in the case of a put. In either case, the minimum margin shall not be less than 100 percent of the option premium received plus 10 percent of the current market value of the equivalent number of shares of the underlying security or the product of the cur-

rent index group value of the underlying index stock group and the applicable index multiplier.

(E)(i) Each put or call shall be margined separately and any difference between the current market value of the underlying security, underlying foreign currency or the current index group value of the underlying index stock group and the exercise price of a put or call shall be considered to be of value only in providing the amount of margin required on that particular put or call. Substantial additional margin must be required on options issued, guaranteed or carried “short” with an usually long period of time to expiration, or written on securities which are subject to unusually rapid or violent changes in value, or which do not have an active market, or where the securities subject to the option cannot be liquidated promptly.

(ii) No margin need be required on any “covered” put or call.

(F)(i) If both a put and call specifying the same number of shares of the same underlying security, the same principal amount of the same United States Government obligation, the same number of units of the same underlying foreign currency or the same index multiplier for the same index stock group are issued, guaranteed or carried “short” for a customer, the amount of margin required shall be the margin on the put or call, whichever is greater, as required pursuant to paragraph (D)(i) above, plus the current market value on the other option. The minimum margin requirement, however, shall not apply to the other option.

(ii) If both a put and call for the same GNMA obligation in the principal amount of \$100,000 are issued, guaranteed or carried

“short” for a customer, the amount of margin required shall be the margin on the put or call, whichever is greater, as required pursuant to paragraph (D)(ii) above, plus the current market value of the other option.

(G)(i) Where a call that is issued by a registered clearing agency is carried “long” for a customer’s account and the account is also “short” a call issued by a registered clearing agency, expiring on or before the date of expiration of the “long” listed call and specifying the same number of shares of the same underlying security, the same principal amount of the same United States Government obligation, the same number of units of the same underlying foreign currency of the same index multiplier for the same index stock group, the margin required on the “short” call shall be the lower of (1) the margin required pursuant to paragraph (D)(i) above, in the case of stock options, United States Government obligations, foreign currency options or index stock group options or (2) the amount, if any, by which the exercise price of the “long” call exceeds the exercise price of the “short” call.

Where a put that is issued by a registered clearing agency is carried “long” for a customer’s account and the account is also “short” a put issued by a registered clearing agency, expiring on or before the date of expiration of the “long” listed put and specifying the same number of shares of the same underlying security, the same principal amount of the same United States Government obligation, the same number of units of the same underlying foreign currency or the same index multiplier for the same index stock group, the margin required on the “short” put shall be the lower of (1) the margin required

pursuant to paragraph (D)(i) above, in the case of stock options, United States Government obligations, foreign currency options or index stock group options or (2) the amount, if any, by which the exercise price of the “short” put exceeds the exercise price of the “long” put.

(ii) Where a call that is issued by a registered clearing agency is carried “long” for a customer’s account and the account is also “short” a call issued by a registered clearing agency, expiring on or before the date of expiration of the “long” listed call and written on the same GNMA obligation in the principal amount of \$100,000, the margin required on the “short” call shall be the lower of (1) the margin required pursuant to subparagraph (f)(2)(D)(ii) above or (2) the amount, if any, by which the exercise price of the “long” call exceeds the exercise price of the “short” call multiplied by the appropriate multiplier factor set forth below.

Where a put that is issued by a registered clearing agency is carried “long” for a customer’s account and the account is also “short” a put issued by a registered clearing agency, expiring on or before the date of expiration of the “long” listed put and written on the same GNMA obligation in the principal amount of \$100,000, the margin required on the “short” put shall be the lower of (1) the margin required pursuant to subparagraph (f)(2)(D)(ii) above or (2) the amount, if any, by which the exercise price of the “short” put exceeds the exercise price of the “long” put multiplied by the appropriate multiplier factor set forth below.

For purposes of this subparagraph (f)(2)(G)(ii), the multiplier factor to be applied shall depend on the then current highest qualifying rate as defined by the rules of the national

securities exchange or national securities association on or through which the option is listed or traded. If the then current highest qualifying rate is less than 8 percent, the multiplier factor shall be 1; if the then current highest qualifying rate is greater than or equal to 8 percent but less than 10 percent, the multiplier factor shall be 1.2; if the then current highest qualifying rate is greater than or equal to 10 percent but less than 12 percent, the multiplier factor shall be 1.4; if the then current highest qualifying rate is greater than or equal to 12 percent but less than 14 percent, the multiplier factor shall be 1.5; if the then current highest qualifying rate is greater than or equal to 14 percent but less than 16 percent, the multiplier factor shall be 1.6; and if the then current highest qualifying rate is greater than or equal to 16 percent but less than or equal to 18 percent, the multiplier factor shall be 1.7. The multiplier factor or factors for higher qualifying rates shall be established by the Association as required.

(H)(i) Where a call is issued, guaranteed or carried “short” against an existing net “long” position in the security under option or in any security immediately exchangeable or convertible, other than warrants, without restriction including the payment of money into the security under option, no margin need be required on the call, provided (1) such net long position is adequately margined in accordance with this Section and (2) the right to exchange or convert the net “long” position does not expire on or before the date of expiration of the “short” call. Where a put is issued, guaranteed or carried “short” against an existing net “short” position in the security under option, no margin need be required on the put, provided such net “short” position is adequately margined in accor-

dance with this Section.

(ii) Where a call representing stock options is issued, guaranteed or carried “short” against an existing net “long” position in a warrant convertible into the underlying security under option, margin shall be required on the call equal to any amount by which the conversion price of the “long” warrant exceeds the exercise price of the call, provided (1) such net long position is adequately margined in accordance with this Section and (2) the right to convert the net “long” position does not expire on or before the date of expiration of the “short” call. However, when a payment of money is required to convert the “long” warrant, such warrant shall have no value for purposes of this Section.

(iii) In determining net “long” and net “short” positions, for purposes of subparagraphs (f)(2)(H)(i) and (ii) above, offsetting “long” and “short” positions in exchangeable or convertible securities (including warrants) or in the same security, as discussed in subsection 3(e)(1) of this Section, shall be deducted. In computing margin on such an existing net security position carried against a put or call, the current market price to be used shall not be greater than the exercise price in the case of a call or less than the current market price in the case of a put and the required margin shall be increased by any unrealized loss.

(iv) Where a put or call is carried “short” in the account of a customer against a letter of guarantee in a form satisfactory to the Association and issued by a third party custodian bank or trust company (the “guarantor”), which letter of guarantee is held in the account at the time the put or call is written, or is received in the account promptly thereafter, no margin need be

required on the put or call.

In the case of a call on a broad index stock group, the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter either (1) cash, (2) cash equivalents, (3) one or more qualified securities, or (4) any combination thereof, having an aggregate market value, computed as at the close of business on the day the call is written, of not less than 100 percent of the aggregate current index value computed as at the same time and that the guarantor will promptly pay the member the exercise settlement amount in the event the account is assigned an exercise notice. The letter of guarantee may provide for substitution of qualified securities held as collateral provided that the substitution shall not cause the value of the qualified securities held to be diminished. A qualified security means (1) an equity security, other than a warrant, right or option, that is traded on any national securities exchange, or (2) any equity security, other than a warrant, listed in the current list of Over-the-Counter Margin Stocks as published by the Board of Governors of the Federal Reserve System.

In the case of a call on any other option contract, the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter, the underlying security (or a security immediately convertible into the underlying security without the payment of money) or foreign currency and that the guarantor will promptly deliver to the member the underlying security or foreign currency in the event the account is assigned an exercise notice.

In the case of a put on an option contract (including a put on a broad

index stock group), the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter, cash or cash equivalents which have an aggregate market value, computed as at the close of business on the day the put is written, of not less than 100 percent of the aggregate exercise price of the put and that the guarantor will promptly pay the member the exercise settlement amount (in the case of a put on a broad index stock group) or the aggregate exercise price (in the case of any other put on an option contract) in the event the account is assigned an exercise notice. Cash equivalents shall mean those instruments referred to in 220.8(a)(3)(ii) of Regulation T of the Board of Governors of the Federal Reserve System.

(I) When a member issues or guarantees an option to receive or deliver securities or foreign currencies for a customer, such option shall be margined as if it were a put or call.

(J) Notwithstanding the other provisions of this subsection 3(f)(2), a member may clear and carry the listed option transactions of one or more registered specialists, registered market makers, or registered traders in options (which registered traders are deemed specialists for all purposes under the Securities Exchange Act of 1934 pursuant to the rules of a national securities exchange), upon a margin basis satisfactory to the concerned parties, provided that all real and potential risks in accounts carried under such arrangements are at all times adequately covered by the margin maintained in the account, or, in the absence thereof, by the carrying member as a charge when computing net capital.

Securities, including options, in such accounts shall be valued con-

servatively in the light of current market prices and the amount which might be realized upon liquidation. Substantial additional margin must be required or excess net capital maintained in all cases where the securities carried: (i) are subject to unusually rapid or violent changes in value including volatility in the expiration months of options, (ii) do not have an active market, or (iii) in one or more or all accounts, including proprietary accounts combined, are such that they cannot be liquidated promptly or represent undue concentration of risk in view of the carrying member's net capital and its overall exposure to material loss.

(K) The Association may at any time impose higher margin requirements with respect to any option position(s) when it deems such higher margin requirements are appropriate.

(3) "When Issued" and "When Distributed" Securities

(A) Margin Accounts — The margin to be maintained on any transaction or net position in each "when issued" security shall be the same as if such security were issued.

Each position in a "when issued" security shall be margined separately and any unrealized profit shall be of value only in providing the amount of margin required on that particular position.

When an account has a "short" position in a "when issued" security and there are held in the account securities upon which the "when issued" security may be issued, such "short" position shall be marked to the market and the balance in the account shall for the purpose of this Section be adjusted for any unrealized loss in such "short" position.

(B) Cash Accounts — On any transaction or net position resulting from contracts for a “when issued” security in an account other than that of a member, non-member broker/dealer, or a “designated account,” equity must be maintained equal to the margin required were such transaction or position in a margin account.

On any net position resulting from contracts for a “when issued” security made for or with a non-member broker/dealer, no margin need be required, but such net position must be marked to the market.

On any net position resulting from contracts for a “when issued” security made for a member or for or with a “designated account,” no margin need be required and such net position need not be marked to the market. However, where such net position is not marked to the market, an amount equal to the loss at the market in such position shall be charged against the member’s net capital as provided in SEC Rule 15c3-1.

The provisions of this paragraph shall not apply to any position resulting from contracts on a “when issued” basis in a security:

(i) which is the subject of a primary distribution in connection with a bona fide offering by the issuer to the general public for “cash,” or

(ii) which is exempt by the Association as involving a primary distribution.

The term “when issued” as used herein also means “when distributed.”

(4) Guaranteed Accounts — Any account guaranteed by another account may be consolidated with such other account and the margin

to be maintained may be determined on the net position of both accounts, provided the guarantee is in writing and permits the member carrying the account, without restriction, to use the money and securities in the guaranteeing account to carry the guaranteed account or to pay any deficit therein; and provided further that such guaranteeing account is not owned directly or indirectly by (a) a member, or any stockholder (other than a holder of freely transferable stock only) in the organization carrying such account or (b) a member, or any stockholder (other than a holder of freely transferable stock only) therein having a definite arrangement for participating in the commissions earned on the guaranteed account. However, the guarantee of a limited partner or of a holder of non-voting stock, if based upon his resources other than his capital contribution to or other than his interest in a member, is not affected by the foregoing prohibition, and such a guarantee may be taken into consideration in computing margin to be maintained in the guaranteed account.

When one or more accounts are guaranteed by another account and the total margin deficiencies guaranteed by any guarantor exceeds 10 percent of the member’s excess net capital, the amount of the margin deficiency being guaranteed in excess of 10 percent of excess net capital shall be charged against the member’s net capital when computing net capital under SEC Rule 15c3-1.

(5) Consolidation of Accounts — When two or more accounts are carried for a customer, the margin to be maintained may be determined on the net position of said accounts, provided the customer has consented that the money and securities in each of such accounts

may be used to carry or pay any deficit in all such accounts.

(6) Time Within Which Margin or “Mark to Market” Must Be Obtained — The amount of margin or “mark to market” required by any provision of this Section shall be obtained as promptly as possible and in any event within fifteen business days from the date such deficiency occurred, unless the Association has specifically granted the member additional time.

(7) Practice of Meeting Regulation T Margin Calls by Liquidation Prohibited — When a “margin call,” as defined in Section 220.2(1) of Regulation T of the Board of Governors of the Federal Reserve System, is required in a customer’s account, no member shall permit a customer to make a practice of either deferring the deposit of cash or securities beyond the time when such transactions would ordinarily be settled or cleared, or meeting the margin required by the liquidation of the same or other commitments in the account.

This prohibition on liquidations shall only apply to those accounts that, at the time of liquidation, are not in compliance with the equity to be maintained pursuant to the provisions of this Section.

(8) Special Initial and Maintenance Margin Requirements —

(A) Notwithstanding the other provisions of this Section, the Association may, whenever it shall determine that market conditions so warrant, prescribe:

(i) higher initial margin requirements for the purpose of effecting new securities transactions and commitments in accounts of customers with respect to specific securities,

(ii) higher maintenance margin requirements for accounts of customers with respect to any securities, and

(iii) such other terms and conditions as the Association shall deem appropriate relating to initial and/or maintenance margin requirements for accounts of customers with respect to any securities.

(B) Day-Trading — The term “day-trading” means the purchasing and selling of the same security on the same day. A “day-trader” is any customer whose trading shows a pattern of day-trading.

Whenever day-trading occurs in a customer’s margin account the margin to be maintained shall be the margin on the “long” or “short” transaction, whichever occurred first, as required pursuant to the other provisions of this Section. When day-trading occurs in the

account of a “day-trader” the margin to be maintained shall be the margin on the “long” or “short” transaction, whichever occurred first, as required by Regulation T of the Board of Governors of the Federal Reserve System or as required pursuant to the other provisions of this Section, whichever amount is greater.

(C) When the equity in a customer’s account, after giving consideration to the other provisions of this Section, is not sufficient to meet the requirements of paragraph (f)(8)(A) or (B) additional cash or securities must be received into the account to meet any deficiency within seven business days of the trade date.

(9) Free Riding in Cash Accounts Prohibited — No member shall permit a customer (other than a broker/dealer or a “designated account”) to make a practice,

directly or indirectly, of effecting transactions in a cash account where the cost of securities purchased is met by the sale of the same securities. No member shall permit a customer to make a practice of selling securities with them in a cash account which are to be received against payment from another broker/dealer where such securities were purchased and are not yet paid for. A member transferring an account which is subject to a Regulation T 90-day freeze to another member firm shall inform the receiving member of such 90-day freeze.

The provisions of Section 220.8(c) of Regulation T of the Board of Governors of the Federal Reserve System dictate the prohibitions and exceptions against customers’ free riding. Members may apply to the Association in writing for waiver of a 90-day freeze not exempted by Regulation T.

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NASD NOTICE TO MEMBERS 93-24

SEC Approves Fifth-Character Identifier In Market-Maker Symbols for Non-Primary Trading Location

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On February 26, 1993, the Securities and Exchange Commission (SEC) approved amendments to Schedule D that require members to append a fifth-character location indicator to their market-maker identification symbol (MMID) in securities that are traded at a location away from the primary trading location. The amendments are effective immediately. The text of the amendments follows the discussion below.

Background and Description of Amendments

The SEC approved a proposal to amend Part VI of Schedule D to the NASD By-Laws to require market makers to use a special identifier for a trading desk located away from the firm's primary office. This fifth character attaches to the MMID that appears on the Nasdaq Workstation screen and alerts market participants to the fact that the trading desk of a member in a particular stock may not be located at the main trading office. Although available for many years, use of the fifth character was voluntary.

The NASD decided to require its use to avoid confusion and delay in contacting the appropriate market maker in a particular security. Using the fifth character will ensure

that traders transacting an order will call the appropriate location where the market maker for the stock is located and avoid making multiple phone calls to execute the trade. The location indicators can be found in the *Nasdaq/CQS Symbol Directory*.

Questions regarding this Notice may be directed to the Market Surveillance Department at (301) 590-6080 or to Beth E. Weimer, Associate General Counsel at (202) 728-6998.

Text of New Rules

(Note: New language is underlined.)

Schedule D

Part VI

Requirements Applicable to Nasdaq Market Makers

* * * * *

(g) In cases where a market making member has more than one trading location, a fifth-character geographic indicator shall be appended to the market maker's identifier for that security to identify the branch location where the security is traded. The fifth-character branch indicators are established by the Association and published from time to time in the Nasdaq/CQS Symbol Directory.

NASD NOTICE TO MEMBERS 93-25

SEC Approves New Trade-Reporting Requirements for Late-Trade Reports

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On March 22, 1993, the Securities and Exchange Commission (SEC) approved amendments to Schedule D, and Schedule G, to the By-Laws and to the Rules of Practice and Procedure for the Automated Confirmation Transaction (ACT) service rules to require members to input the time of execution on late-trade reports and to add a section regarding audit-trail data. The amendments are effective immediately. The text of the amendments follows the discussion below.

Background and Description of Amendments

The SEC has approved amendments to Schedules D and G and the ACT Rules to require members to append the time of execution on any trade report that is reported more than 90 seconds after execution. The NASD is also modifying the ACT Rules to reflect the same time-of-execution requirements and to adopt an "audit trail" provision. The proposals will enable the NASD to capture accurate audit trail information for surveillance purposes and will also facilitate market surveillance of member compliance with the proposed Nasdaq short-sale rule or "bid test" should the SEC approve that proposal.¹

• **Audit Trail Provision** — The NASD has a statutory responsibility to surveil trading in its marketplace for potential violations of the securities laws and the NASD's own rules. To discharge this responsibility, the NASD relies on computerized analyses of trade details reported by member firms through the trade-reporting and trade-clearance processes. Once processed, this transactional data forms the NASD's transaction audit trail, a

critical function supporting the NASD's market surveillance and enforcement programs. Hence, members' submission of accurate and complete audit-trail information is essential.

During the past two years, the NASD's ACT service has evolved to permit the capture of trade-by-trade information for virtually all segments of the NASD's marketplace. Designed as the mechanism to compare and lock in the terms of telephonically negotiated trades in Nasdaq securities, the ACT service also processes transactions in exchange-listed (CQS) securities traded over-the-counter, and non-Nasdaq securities that clear through NSCC.² In addition, the trade-reporting systems that were stand-alone systems before ACT's development are now part of the ACT service, so that members must report into ACT internalized transactions and trades executed and compared in their internal systems. Because ACT facilitates the collection and dissemination of all reportable real-time trade reports for Nasdaq National Market securities, Nasdaq SmallCap securities, and exchange-listed securities, it offers the capability to gather complete audit-trail information for

¹The NASD has proposed a short-sale rule for Nasdaq National Market securities (SR-NASD-92-12).

²In File No. SR-NASD-92-5, the NASD obtained SEC approval of the following changes to the ACT Rules:

(1) expanding the definition of "ACT eligible security" to include all OTC securities not traded on Nasdaq that are eligible for clearing with NSCC;

(2) expanding the definition of "reportable ACT transaction" to include internalized trades and transactions effected in members' proprietary execution systems.

every trade in a single input process. Accordingly, the NASD is amending the ACT rules to provide an audit-trail provision.

• **Time of Execution** — Ensuring that trade reports are properly time sequenced is critical to constructing an accurate audit trail for surveillance purposes. At present, however, there is no effective manner to sequence properly transactions reported as “.SLD” (i.e., not reported within 90 seconds after execution). The NASD performs many surveillance functions, both on-line and off-line, that require accurate sequencing of trade report data and knowledge of the time of execution for investigations of questionable trading activity. For exchange-listed securities, time of execution appended to late-trade reports will also enable the NASD to respond more expeditiously and completely to inquiries from exchanges dealing with late-trade reports and trade-through allegations.

Knowing the time of trade executions is also crucial to initiate on-line monitoring for compliance with the proposed Nasdaq bid test. The NASD believes that comprehensive monitoring of member compliance with the bid test is necessary to ensure the credibility of the bid test itself while providing for the capability to respond immediately to situations requiring further investigation and analysis. Accordingly, the NASD has determined that members must report through ACT the time of execution of a transaction not reported within 90 seconds.

Although “time of execution” is an existing ACT field, its use was voluntary. To develop and maintain an accurate audit trail, the NASD has amended the rules to require that members use the time-of-execution

field in ACT when submitting trade reports to the NASD more than 90 seconds after an execution.³

Questions regarding this Notice may be directed to the Market Surveillance Department at (301) 590-6080 or to Beth E. Weimer, Associate General Counsel at (202) 728-6998.

Text of New Rules

(Note: New language is underlined; deleted text is in brackets.)

Schedule D

Part XII

Reporting Transactions in Nasdaq National Market System Securities

Section 2 — Transaction Reporting

(a) When and How Transactions are Reported

(1) Registered Reporting Market Makers shall, within 90 seconds after execution, transmit through ACT last sale reports of transactions in designated securities executed during normal market hours. Transactions not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

(2) Non-Registered Reporting Members shall, within 90 seconds after execution, transmit through ACT or the ACT service desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to the Market Operations Department in New York City, last sale reports of transactions in designated securities executed during normal market hours. Transactions

not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

* * * * *

(4) Last sale reports of transactions in designated securities executed between the hours of 4:00 p.m. and 5:15 p.m. Eastern Time shall be transmitted through ACT within 90 seconds after execution; trades executed and reported after 4:00 p.m. Eastern Time shall be designated as “.T” [or after hours] trades to denote their execution outside normal market hours. Transactions not reported within 90 seconds must include the time of execution on the trade report.

(5) All members shall report weekly to the Market Operations Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities executed outside the hours of 9:30 a.m. and 5:15 p.m. Eastern Time.

* * * * *

(c) Information To Be Reported

Each last sale report shall contain the following information:

- (1) Nasdaq symbol of the designated security;
- (2) Number of shares, excluding odd lots;

³If, however, a member submits trade reports to the NASD in a timely manner and a system error or computer connection failure causes the trade reports to arrive at the NASD more than 90 seconds after execution, the member may contact the Market Surveillance Department to request an exemption to the time-of-execution requirement.

(3) Price of the transaction as required by paragraph (d) below;

(4) A symbol indicating whether the transaction is a buy, sell, or cross;

(5) The time of execution if the trade is reported more than 90 seconds after execution.

Part XIII

Reporting Transactions in Nasdaq SmallCap Securities

Section 2 — Transaction Reporting

(a) When and How Transactions are Reported

(1) Registered Reporting Market Makers shall, within 90 seconds after execution, transmit through ACT last sale reports of transactions in designated securities executed during normal market hours. Transactions not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

(2) Non-Registered Reporting Members shall, within 90 seconds after execution, transmit through ACT or the ACT service desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to the Market Operations Department in New York City, last sale reports of transactions in designated securities executed during normal market hours. Transactions not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

* * * * *

(4) Last sale reports of transactions

in designated securities executed between the hours of 4:00 p.m. and 5:15 p.m. Eastern Time shall be transmitted through ACT within 90 seconds after execution; trades executed and reported after 4:00 p.m. Eastern Time shall be designated as “.T” [or after hours] trades to denote their execution outside normal market hours. Transactions not reported within 90 seconds must include the time of execution on the trade report.

(5) All members shall report weekly to the Market Operations Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities executed outside the hours of 9:30 a.m. and 5:15 p.m. Eastern Time.

* * * * *

(c) Information To Be Reported

Each last sale report shall contain the following information:

(1) Nasdaq symbol of the designated security;

(2) Number of shares, excluding odd lots;

(3) Price of the transaction as required by paragraph (d) below;

(4) A symbol indicating whether the transaction is a buy, sell, or cross;

(5) The time of execution if the trade is reported more than 90 seconds after execution.

* * * * *

Schedule G

Section 2 — Transaction Reporting

(a) When and How Transactions are Reported

(1) Registered Reporting Members shall transmit through ACT, within 90 seconds after execution, last sale reports of transactions in eligible securities executed during the trading hours of the Consolidated Tape otherwise than on a national securities exchange. Registered Reporting Members shall also transmit through ACT, within 90 seconds after execution, last sale reports of transactions in eligible securities executed in the United States otherwise than on a national securities exchange between 4:00 p.m. and 5:15 p.m. Eastern Time. Transactions not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

(2) Non-Registered Reporting Members shall, within 90 seconds after execution, transmit through ACT or the ACT service desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to the Market Operations Department in New York City, last sale reports of transactions in eligible securities executed during the trading hours of the Consolidated Tape otherwise than on a national securities exchange.

Non-registered Reporting Members shall, within 90 seconds after execution, transmit through ACT or the ACT service desk (if qualified pursuant to Part IX of Schedule D to the By-Laws), or if ACT is unavailable due to system or transmission failure, by telephone to Market Operations Department in New York City, last sale reports of transactions in eligible securities executed in the United States otherwise than on a national securities

exchange between the hours of 4:00 p.m. and 5:15 p.m. Eastern Time. Transactions not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

* * * * *

(c) Information To Be Reported

Each last sale report shall contain the following information:

- (1) Stock symbol of the eligible security;
- (2) Number of shares (odd lots shall not be reported);
- (3) Price of the transaction as required by paragraph (d) below;
- (4) A symbol indicating whether the transaction is a buy, sell, or cross;

(5) The time of execution if the trade is reported more than 90 seconds after execution.

* * * * *

ACT Rules

* * * * *

(d) TRADE REPORT INPUT

* * * * *

4. Trade information to be input — Each ACT report shall contain the following information:

- (A) Security identification symbol of the eligible security (“SECID”);
- (B) Number of shares;
- (C) Unit price, excluding commissions, mark-ups, or mark-downs;
- (D) Execution time for any transac-

tion in Nasdaq or CQS securities not reported within 90 seconds of execution;

Subsections (D) through (K) redesignated (E) through (L) respectively.

* * * * *

(h) Audit Trail Requirements

The data elements specified in paragraph (d)(4) are critical to the Association’s compilation of a transaction audit trail for regulatory purposes. As such, all member firms utilizing the ACT Service have an ongoing obligation to input paragraph (d)(4) information accurately and completely.

Sections (h) and (i) redesignated as Sections (i) and (j) respectively.

NASD NOTICE TO MEMBERS 93-26

NASD Urges Members to Provide Complete and Accurate Blue Sheet Submissions

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD urges members to take immediate action to ensure the accuracy and completeness of trading data submitted through the NASD's electronic blue sheet system in response to regulatory inquiries. The NASD has become concerned that the quality of submissions by members is not at an acceptable level. Among the problems are improper reporting and formatting of information; missing data; timeliness; and failure to provide all of the required information. Because complete, accurate, and timely trading data properly formatted is crucial to the NASD investigative process, continued failure to meet these requirements may result in review and possible disciplinary action by the District Business Conduct and Market Surveillance Committees. In addition to addressing the various problems encountered by NASD staff with submissions of trading data, this Notice also provides members with certain clarifications concerning the submissions.

Background

Since February 12, 1989, Part VI, Section 4 of Schedule D and Section 3 of Schedule H of the NASD's By-Laws have required members to submit trading data to the NASD in a standardized, automated format when responding to an NASD investigative request. The NASD employs the same automated format developed jointly with the New York Stock Exchange (NYSE), the Securities Industry Association (SIA), and the Securities and Exchange Commission (SEC).

Notice to Members 89-70 described several problems that the NASD experienced with the accuracy of

the trading information that members were submitting electronically. Several serious problems still exist with not only the accuracy of the information received by the NASD, but also the timeliness of responses and the reporting format. These problems impair the NASD's ability to use the trading information for investigative purposes and result in additional requests for information that cause unacceptable time delays and create unnecessary burdens on both NASD staff and members. Therefore, members must take immediate action to ensure that the trading data submitted to the NASD through its electronic blue sheet systems is complete and accurate.

Members must make complete and accurate reporting within specified time frames. A response is not complete unless all the required fields, detailed in *Notice to Members 89-17*, have been provided in the appropriate format. Members must correct any deficiencies the NASD discovers when validating the data. Continued failure to submit complete and accurate trading data on a timely basis in the proper format will result in review and probable disciplinary action by the District Business Conduct and Market Surveillance Committees.

To help members properly submit trading data, certain clarifications regarding problem areas are discussed below along with the appropriate method of submission.

Definitions, Explanations, And Modifications

1. Submitting Broker Number — National Securities Clearing Corporation (NSCC) members submitting data should use their NSCC clearing number. Non-NSCC members submitting data should use the clearing number assigned by their

clearing agency.

2. Requesting Organization

Number — This NASD-assigned number is most often found on the reference line of the NASD's request letter. *Firms must submit the number precisely as it appears on the request letter.*

3. Requestor Code — For SIAC submissions, firms must input the appropriate requestor code for the trading data to reach the organization that requested it. *The NASD's requestor code, "R", must be used when submitting automated trading data for the NASD.*

4. Opposing Broker Number — The opposing broker number should reflect the NSCC clearing number of the broker/dealer on the other side of the trade. (For a principal trade between a firm and one of its customers, the opposing broker is the firm itself.) If the opposing broker/dealer is not an NSCC member, use the number assigned by the opposing broker/dealer's clearing agency.

Never leave this field blank.

5. Buy/Sell Code — Determine the buy/sell code from the *perspective of the account listed in the name and address fields*. The following values represent the appropriate transaction: 0=Buy, 1=Sale, 2=Short Sale, A=Buy Cancel, B=Sale Cancel, and C=Short Sale Cancel. Values 3 to 6 and D through G are for options transactions only.

****All Trade Corrections and Cancellations Must Be Provided****

6. Price — Express the transaction price as a decimal value. For example, 3 1/8 = 3.125. Format: \$\$\$\$CCCCC.

7. Exchange Code — The exchange code reflects the market where a transaction was executed. For example, a firm may execute trades in a Nasdaq security away from the Nasdaq market place. Should this be the case, the additional trades executed away from the primary market must also be submitted. Blue Sheet responses must include *all* transactions executed by the member submitting the data and by all correspondent firms for which that member clears, in the security(ies) requested, regardless of where the trade was executed. Using the market codes listed below, the firm should indicate where the trade was executed.

Market Codes:

A = New York Stock Exchange
B = American Stock Exchange
C = Midwest Stock Exchange
D = Philadelphia Stock Exchange
E = Pacific Stock Exchange
F = Boston Stock Exchange
G = Cincinnati Stock Exchange
K = Chicago Board Options Exchange
L = London (OTC or Exchange)
M = Toronto Stock Exchange
N = Montreal Stock Exchange
O = Vancouver Stock Exchange
Q = POSIT
R = Nasdaq
S = Domestic (OTC)
T = Tokyo (OTC or Exchange)
U = Instinet
W = Arizona Stock Exchange
Y = Other-Domestic
Z = Other-Foreign

8. Broker/Dealer Code — The broker/dealer code indicates if the trade was for the submitting firm *or* its correspondent.

0 = Trade for the submitting firm or a customer of the submitting firm.

1 = Trade for a correspondent of the submitting firm or a customer of the correspondent firm.

9. State Code — The state code must be the standard postal two-character identification. This field must reflect the state as listed in the name and address fields.

10. Short Name — The short name field should contain an abbreviation of the account name listed in the name and address fields. For retail customers, the short name field should contain the customer's last name, followed by a comma, and then as much of the first name as the remaining field length allows. For wholesale trades, the short name field should contain an abbreviation of the proprietary account listed in the name and address fields.

Never leave this field blank.

11. Proprietary-Customer Indicator — The proprietary-customer indicator identifies whether it is an *agency or principal* transaction.

Values:

1 = Trade was executed on a principal basis involving a *proprietary account* of the submitting firm or one of its correspondent firms.

2 = Trade was executed on an agency basis for a customer of the submitting firm or a customer of the correspondent firm. In both cases a member firm has acted as agent to the customer.

The proprietary-customer indicator must agree with the customer confirmation.

The attached matrix detailing the five different types of trade situations — principal, wholesale, in-house, dual-agency cross, and agency — summarizes much of the information noted above.

Member's Responsibility

The submitting firm must ensure that the NASD receives answers to its requests for trading information within the standard 10 business-day time limit. Similarly, member firms are responsible for the accuracy, formatting, completeness, and timely receipt by the NASD of data submitted for them by service bureaus. Incomplete submissions do not fulfill a member's obligations to make timely reports.

Firms must submit a separate tape, diskette, or SIAC transmission for each blue sheet request they receive.

A member's blue sheet response is not complete unless all of the required fields, *as detailed in Notice to Members 89-17 and elaborated on in this Notice*, have been provided in the appropriate format.

All member firms clearing for introducing firms must identify to the NASD the correspondent firm for which the trading information is being submitted. To facilitate compliance, members may furnish the staff with a key to identify such correspondent firms.

Clearing firms can send copies of these correspondent firm identification lists to the following contact:

Systems Administrator
NASD Market Surveillance
9513 Key West Avenue
Rockville, Maryland 20850
(301) 590-6410.

The NASD has established this Systems Administrator position to assist members with their submissions by responding to questions and concerns regarding the blue sheet process. Also, copies of *Notices to Members 88-104, 89-17, and 89-70* are available to members without charge by contacting the Systems Administrator.

NASD NOTICE TO MEMBERS 93-27

Memorial Day: Trade Date-Settlement Date Schedule

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

The Nasdaq Stock MarketSM and the securities exchanges will be closed on Monday, May 31, 1993, in observance of Memorial Day. "Regular way" transactions made on the preceding business days will be subject to the settlement date schedule listed below.

<u>Trade Date</u>	<u>Settlement Date</u>	<u>Reg. T Date*</u>
May 21	May 28	June 2
24	June 1	3
25	2	4
26	3	7
27	4	8
28	7	9
31	Markets Closed	—
June 1	8	10

Brokers, dealers, and municipal securities dealers should use these settlement dates to clear and settle transactions pursuant to the NASD Uniform Practice Code and Municipal Securities Rulemaking Board Rule G-12 on Uniform Practice.

Questions regarding the application of these settlement dates to a particular situation may be directed to the NASD Uniform Practice Department at (212) 858-4341.

*Pursuant to Sections 220.8(b)(1) and (4) of Regulation T of the Federal Reserve Board, a broker/dealer must promptly cancel or otherwise liquidate a customer purchase transaction in a cash account if full payment is not received within seven (7) business days of the date of purchase or, pursuant to Section 220.8(d)(1), make application to extend the time period specified. The date by which members must take such action is shown in the column entitled "Reg. T Date."

NASD NOTICE TO MEMBERS 93-28

As of March 23, 1993, the following 55 issues joined the Nasdaq National Market,[®] bringing the total number of issues to 3,032:

Nasdaq National Market[®]
Additions, Changes,
And Deletions as of
March 23, 1993

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Symbol	Company	Entry Date	SOES Execution Level
CMPO	Campo Electronics Appliances & Computers Inc.	2/24/93	1000
FSOU	First Southern Bancorp, Inc.	2/24/93	500
PENVF	Philip Environmental Inc.	2/24/93	1000
BOCI	Boca Research, Inc.	2/25/93	1000
RFEDP	Roosevelt Financial Group, Inc. (Pfd)	2/25/93	1000
VFSB	Virginia First Savings Bank, F.S.B.	2/25/93	1000
WFCI	Winston Furniture Company, Inc.	2/25/93	1000
NATH	Nathan's Famous, Inc.	2/26/93	500
TCNOF	Tecnomatix Technologies Ltd.	2/26/93	1000
WHIN	Washington Homes, Inc.	2/26/93	1000
BCIS	Bancinsurance Corporation	3/1/93	1000
HUBC	HUBCO, Inc.	3/1/93	500
JMARW	JMAR Industries, Inc. (2/17/98 Wts)	3/1/93	500
PCBC	Penn Central Bancorp, Inc.	3/3/93	200
CBBI	CB Bancshares, Inc.	3/4/93	200
REIN	Recovery Engineering, Inc.	3/4/93	1000
RSND	Resound Corporation	3/4/93	200
EQCC	EquiCredit Corporation	3/5/93	1000
LSTR	Landstar System, Inc.	3/5/93	1000
SIII	S3 Incorporated	3/5/93	1000
USCN	U.S. Can Corporation	3/8/93	1000
CHCC	Community Health Computing Corp.	3/9/93	1000
INTCW	Intel Corporation (3/9/98 Wts)	3/9/93	1000
SCON	Superconductor Technologies Inc.	3/9/93	200
TNCR	Tencor Instruments	3/9/93	1000
NCSIV	National Convenience Stores Inc.	3/10/93	1000
SBTVF	Scandinavian Broadcasting Systems SA	3/10/93	1000
VICL	Vical Incorporated	3/10/93	500
SPBI	Specialty Paperboard, Inc.	3/11/93	1000
ARSN	AirSensors, Inc.	3/12/93	500
ARSNW	AirSensors, Inc. (3/10/96 Wts)	3/12/93	500
AVID	Avid Technology, Inc.	3/12/93	1000
BRCK	Brock Candy Company (CI A)	3/12/93	1000
ENBC	Energy BioSystems Corporation	3/12/93	1000
FSBXW	Framingham Savings Bank (1/31/96 Wts)	3/12/93	500
INTU	Intuit Inc.	3/12/93	1000
SEHI	Southern Energy Homes, Inc.	3/12/93	1000
ASEC	Aseco Corporation	3/16/93	1000
MWRK	Mothers Work, Inc.	3/16/93	1000
PSUN	Pacific Sunwear of California, Inc.	3/16/93	200
SCVL	Shoe Carnival, Inc.	3/16/93	1000

Symbol	Company	Entry Date	SOES Execution Level
WALL	Wall Data Incorporated	3/16/93	1000
LOMK	Lomak Petroleum, Inc.	3/18/93	1000
MARN	Marion Capital Holdings, Inc.	3/18/93	1000
SPEI	Savoy Pictures Entertainment, Inc.	3/18/93	500
AMTL	AMTROL Inc.	3/19/93	1000
ALMO	Alamo Group, Inc.	3/19/93	1000
MGAW	McGaw, Inc.	3/19/93	1000
MCHP	Microchip Technology Incorporated	3/19/93	1000
TRCD	Tricord Systems, Inc.	3/19/93	200
BKCS	BKC Semiconductor Incorporated	3/22/93	500
CHEZ	Suprema Specialties, Inc.	3/22/93	1000
MAGSF	Magal Security Systems Ltd.	3/23/93	1000
PHCC	Preferred Health Care Ltd.	3/23/93	1000
WCTI	WCT Communications, Inc.	3/23/93	1000

Nasdaq National Market Symbol and/or Name Changes

The following changes to the list of Nasdaq National Market securities occurred since February 23, 1993:

New/Old Symbol	New/Old Security	Date of Change
SMTSZ/SMTSZ	Somanetics Corp. (9/28/93 Wts B)/Somanetics Corp (2/24/93 Wts B)	2/25/93
MDST/MDST	The MEDSTAT Group, Inc./MEDSTAT Systems, Inc.	2/26/93
RCORF/RCORF	Quality Dino Entertainment Ltd./R-Tek Corp.	3/1/93
BPIE/BPIE	BPI Packaging Technologies, Inc./BPI Environmental Inc.	3/2/93
BPIEW/BPIEW	BPI Packaging Technologies, Inc. (Wts A)/BPI Environmental Inc. (Wts A)	3/2/93
BPIEZ/BPIEZ	BPI Packaging Technologies, Inc. (Wts B)/BPI Environmental Inc. (Wts B)	3/2/93
HOMF/HOMF	Home Federal Bancorp/Home Federal Savings Bank	3/2/93
BKUNA/BKUNA	BankUnited Financial Corp. (CI A)/BankUnited, a Savings Bank (CI A)	3/8/93
TSAR/RCDC	Tristar Corp./Ross Cosmetics Distribution Centers, Inc.	3/18/93

Nasdaq National Market Deletions

Symbol	Security	Date
ELMF	Elm Financial Services, Inc.	2/23/93
SMTSZ	Somanetics Corp. (3/20/96 Wts B)	2/24/93
ADVO	ADVO, Inc.	2/25/93
INFM	Inforum, Inc.	2/26/93
NSBA	National Savings Bank of Albany	2/26/93
SECF	Security Financial Holding Co.	2/26/93
ALPC	Allmerica Property & Casualty Companies, Inc.	3/1/93
KCSE	KCS Energy, Inc.	3/1/93
PFBK	Pioneer Savings Bank	3/1/93
DMBK	Dominion Bankshares Corp.	3/2/93

Symbol	Security	Date
JNBK	Jefferson National Bank	3/2/93
ALDN	Alden Press Co.	3/3/93
PICC	Piccadilly Cafeterias, Inc.	3/3/93
DVRS	Diversco, Inc.	3/12/93
FFUT	First Federal Savings Bank	3/15/93
FLGLA	Flagler Bank Corp. (Cl A)	3/15/93
PNTAP	Pentair Inc. (Pfd)	3/15/93
BMJFR	BMJ Financial Corp. (3/15/93 Rts)	3/16/93
CFNE	Circle Fine Art Corporation	3/17/93
HEKN	Heekin Can, Inc.	3/22/93
FRMT	Fremont General Corp.	3/23/93

Questions regarding this Notice should be directed to Mark A. Esposito, Supervisor, Market Listing Qualifications, at (202) 728-8002. Questions pertaining to trade-reporting rules should be directed to Bernard Thompson, Assistant Director, NASD Market Surveillance, at (301) 590-6436.

NASD BOARD BRIEFS

Actions Taken by the NASD Board of Governors in March

• **President's Report** — Nasdaq's performance early in 1993 shows no signs of letup from the record setting pace of 1992. Average daily volume in January was 259.4 million with February's average registering 261.9 million shares a day. Both months were significantly ahead of 1992's record 190.8 million average daily share volume. Average daily dollar volume of \$5.7 billion at the end of February was nearly 63 percent above the average for all of 1992. Total share volume was 10.2 billion by the end of February and represents 21 percent of 1992's all-time record of 48.5 billion shares. Although these numbers reflect a strong and active market, they do not tell the whole story. Indeed, the NASD will be addressing several significant quality-of-market issues in the coming months.

Concern over the impact of the Small Order Execution System (SOES) on volatility and liquidity has led the Board to approve interim and long-term changes to the service. The interim changes would make four primary modifications to SOES: permit market makers to update automatically their quotations after execution; reduce the maximum trade size from 1,000 shares to 500; reduce the required exposure limits for market makers from five to two executions at the displayed price at size limits for each security; and prohibit short sales in SOES. The long-term changes would provide the potential for price improvement, expand limit-order protection, and revise order execution procedures. These improvements will be filed with the SEC for approval.

Under the proposal, investors' limit orders entered into the system within the spread would be interactive, thus increasing the potential for investors to realize price improve-

ment. Price improvement could take place when there is a limit order held in the SOES limit-order file at a price superior to the best bid or ask displayed on Nasdaq. The next incoming market order would be executed at that superior price. If the market maker elected not to execute the order, the system would then execute the market and limit orders against each other.

The modifications would also address the activities of a growing number of professional traders who have been employing the SOES system for trading rather than investing purposes. Under the revised system, all market orders would be guaranteed an execution. Incoming orders would be routed electronically to a market maker quoting at the best price. Currently, a market-making firm has no knowledge of an order until it receives an execution report. The market maker would be able either to accept the order immediately; do nothing, thereby allowing the system to execute it automatically after 15 seconds have elapsed; or reject the order if the market maker had just completed another transaction at the best price and updated its quote. If rejected, the order is then exposed to other competing market makers for execution.

Another ongoing issue is the proposed Nasdaq short-sale rule that would prohibit members from selling short at or below the bid when the current inside or best bid is below the previous inside bid. The proposal has generated a significant amount of comment since its publication in the *Federal Register*. The SEC is reviewing the more than 400 comment letters it has received. This is a complex and difficult issue that both the industry and the SEC are struggling to resolve in the best interest of issuers and the investing public.

Arbitration is another issue to which the NASD will continue to devote considerable time and effort. A major concern is the role punitive damages play in the overall arbitration process and their effect on participants in that process. In addition, the NASD is reviewing the entire arbitration process with the goal of enhancing it as a dispute resolution program for members and public investors.

The NASD and five other securities industry self-regulatory organizations (SROs) have agreed to develop a single continuing education program for all securities industry registered representatives and principals. Further, the NASD has agreed to remain flexible on the question of whether to include an assessment component in any continuing education program. An 11-person task force will report back to the six SROs by mid-year with recommendations for implementing the program. The Board expects to act on these recommendations by year-end with implementation of an acceptable program anticipated in early 1994.

In the area of legislation, there has been relatively little activity due to the uncertainty over the direction of the new administration and the question of SEC Chairman Richard Breeden's successor. Congress will probably defer action on the Government Securities Reform Act of 1993 pending appointment of an SEC Chairman and other high officials at the Treasury Department. This Act would provide the NASD with authority to regulate the sales practices of government securities dealers. Legislation that would authorize the SEC to delegate investment adviser examination responsibilities to the NASD for certain of its members will be marked up in several weeks. There is a good chance of success in this

area as the NASD has attempted to resolve concerns expressed by both the International Association for Financial Planning (IAFP) and the SEC.

• **Market Services** — Nasdaq market makers identify trades in exchange-listed securities executed away from the inside or closing market price and after 4 p.m. with a “.W”. Use of this indicator denotes that the member reported the trade at a price based on an averaged-weighting or other formula rather than a current negotiated price. The Board has approved for filing with the SEC a rule change that would apply this indicator to such average-priced trades in Nasdaq securities as well as exchange-listed securities. The Board also agreed that the Trading Committee should further review the policy issues raised by average-priced trades.

The Board approved the development of a new section to the Uniform Practice Code to require members to use uniform procedures regarding how to handle open customer limit orders when market makers quote the securities ex-dividend, ex-distribution, ex-rights, or ex-interest. Once developed, the NASD will file these measures with the SEC for approval. Currently, members differ in their handling of these orders. Some adjust the price of the order by the “ex” amount, while others do nothing and execute the orders at a higher cost per share than would have been the case with the price adjustment. As a result, the NASD Board determined to require members to process open orders and limit orders according to uniform procedures, to avoid customer confusion and inequitable treatment.

Modifications to the Computer Assisted Execution System (CAES) have received Board approval. One

measure would modify the execution process to execute orders automatically at the market makers' quote and up to its posted size only when that quote equals the inside quote from all listed markets. Currently CAES executes orders up to 1,000 shares at the inside Consolidated Quotation System (CQS) quote (including exchange markets) regardless of the market maker's individual CAES quote. The change would address situations where the exchange quote is the inside market but the CAES market maker displays a different quotation. The CAES order would not be automatically executed at the inside, but would appear on the market maker's screen for manual acceptance at the inside quote.

Another proposal would require the pricing of all CAES orders input during the trading. This change would eliminate market orders being rejected by a CAES market maker who does not want to honor a stale inside quote (i.e., a quote from an exchange floor that does not reflect the current price). Additionally, CAES would not accept odd-lot orders. The proposal also includes a provision for eliminating the rounding of quotations in CQS securities. Currently, CAES rounds quotations of 1/16th point to 1/8th point, which may cause the third market to lock an exchange-market quotation.

A number of changes proposed to improve the OTC Bulletin Board service received Board approval. One change would impose minimum-size standards on firm bid and offer prices in the Bulletin Board. The proposed standards for determining the minimum quote sizes are:

Price (Bid or Offer)	Minimum Quote Size
\$0.00 to \$.50	5,000
\$.51 to \$1.00	2,500
\$1.01 to \$10.00	500
\$10.01 to \$100.00	200
\$100.01 to \$200.00	100
\$200.01 or more	50

Other proposed changes include a 90-second-trade-reporting capability for all over-the-counter securities not traded on Nasdaq, display of last sale and volume on the Bulletin Board, a short-form quote updating capability, and a ticker capability for Bulletin Board securities.

Changes to the rules governing the operation of the Bulletin Board also received Board approval. These rule changes include modifying the definition of Bulletin Board eligible securities to permit inclusion of equities listed on regional exchanges that do not qualify for transaction reporting through the Consolidated Tape and to include issues that the American and New York stock exchanges have suspended pending delisting.

The Board approved filing for an extension of the policy banning autoquoting in Nasdaq. The Board's policy prohibits systems known as "autoquote" systems from effecting automated quotation updates or

tracking of inside quotations in Nasdaq with two exceptions: automated update of quotations is permitted when the update is in response to an execution in the security; and automated update is permitted when it requires a physical entry to the market maker's internal system that then automatically forwards the update to Nasdaq.

Pending SEC approval, the NASD will grant the West Canada Depository Company access to the Automated Confirmation Transaction (ACT) service to compare trades. The depository company represents a number of Canadian non-member broker/dealers that trade with NASD members.

• **Regulation** — The Board approved for distribution to the members a Notice clarifying the application of the Corporate Financing Rule to merger and acquisition transactions. Basically, members do not have to file cash tender offers, cash mergers, cash tender offers followed by a stock or cash-election merger, and spin-offs. Because exchange offers with existing shareholders and stock-for-stock merger transactions involve a member's participation in a distribution, members should file these with the NASD.

The NASD will file shortly with the SEC recommended procedures to facilitate compliance with the requirement that the NASD be informed when a market maker elects to act as a passive market maker. These changes will be filed as amendments to a proposal that the NASD currently has pending at the SEC. The filing under consideration would amend Schedule D to prevent inadvertent violations of the two- and nine-day cooling-off periods mandated by Rule 10b-6.

The proposed amendment contemplates a procedure whereby market makers would be granted excused withdrawals from Nasdaq market making based on notification by the manager to Nasdaq Operations that such market makers intend to participate in a public offering. The NASD proposed the amendment after the SEC staff alerted the NASD that members engaged in the distribution of securities of companies listed in The Nasdaq Stock Market are, through inadvertence or otherwise, not always complying with the provisions of the 10b-6 cooling-off periods. Accordingly, the NASD proposed its Schedule D changes to provide a mechanism to assist market makers in complying with the Rule.

DISCIPLINARY ACTIONS

Disciplinary Actions Reported for April

The NASD® is taking disciplinary actions against the following firms and individuals for violations of the NASD Rules of Fair Practice; securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board. Unless otherwise indicated, suspensions will begin with the opening of business on Monday, April 19, 1993. The information relating to matters contained in this Notice is current as of the fifth of this month. Information received subsequent to the fifth is not reflected in this publication.

Firms and Individuals Fined

Dillon Securities, Inc. (Spokane, Washington) and **Lyle R. Haas (Registered Principal, Spokane, Washington)**. Dillon Securities was fined \$20,000, and Haas was fined \$10,000 and required to requalify by examination as a financial and operations principal. The SEC affirmed the sanctions following an appeal of an October 1988 NBCC decision. The sanctions were based on findings that the firm and Haas failed to prepare accurate net capital computations for certain periods. The respondents also failed to transmit promptly investor checks received in two best-efforts underwritings to a separate escrow account.

Individuals Barred or Suspended

Keith A. Bergner (Registered Representative, Lakewood, Colorado) was fined \$5,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 3 District Business Conduct Committee (DBCC) decision. The sanctions were based on findings that Bergner failed to pay a

\$31,733.34 NYSE arbitration award.

Tomas Bernardino (Registered Representative, Philadelphia, Pennsylvania) submitted an Offer of Settlement pursuant to which he was fined \$4,965 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Bernardino consented to the described sanctions and to the entry of findings that he received from a public customer \$993 in insurance premiums but failed to remit the monies to his member firm.

John A. Bochetto (Registered Representative, Rochester, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$25,000, barred from association with any NASD member in any capacity, and required to pay \$1,000 in restitution to his member firm. Without admitting or denying the allegations, Bochetto consented to the described sanctions and to the entry of findings that he misappropriated and converted to his own use customer funds totaling \$1,000 intended for the purchase of shares of a mutual fund. In addition, the findings stated that Bochetto failed to respond to NASD requests for information.

Gregory Dean Boynton (Registered Representative, Walnut, California) was fined \$14,283.62, suspended from association with any NASD member in any capacity for 10 business days, and required to requalify by examination. The NBCC imposed the sanctions following an appeal of a District 1 DBCC decision. The sanctions were based on findings that Boynton effected unauthorized transactions in two customer accounts.

Joseph R. Callaghan (Registered Representative, Beaver, Pennsylvania) submitted an Offer of Settlement pursuant to which he was fined \$30,000, barred from association with any NASD member in any capacity, and required to pay \$31,000 in restitution to customers. Without admitting or denying the allegations, Callaghan consented to the described sanctions and to the entry of findings that he received \$31,000 from public customers for investment purposes, or for repaying an insurance policy loan, failed to use the funds for their intended purposes, and converted the monies to his own use and benefit.

Jeffery W. Caudill (Registered Representative, Midlothian, Virginia) submitted an Offer of Settlement pursuant to which he was fined \$60,000 and barred from association with any NASD member in any capacity. In addition, Caudill is required to pay \$24,900 in restitution to investors. Without admitting or denying the allegations, Caudill consented to the described sanctions and to the entry of findings that he engaged in private securities transactions without notifying his member firm, and submitted to customers a private placement offering memorandum and an addendum containing inaccurate disclosures, misstatements, and omissions of material facts. The NASD also determined that Caudill failed to provide investors with a prospectus or any additional information regarding the offering.

The findings also stated that Caudill, through the use of sales literature, advertisements, and other forms of communications, held a firm out to the public and permitted persons associated with the firm to hold it out to the public as an independent broker/dealer, when it could not lawfully act as one.

According to the findings, this firm, acting through Caudill, raised \$115,000 from eight investors intended for investment in the aforementioned private offering and that Caudill converted \$24,900 of the investors' funds to his own use and benefit.

Charles R. Cavallaro (Registered Representative, Sewell, New Jersey) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Cavallaro consented to the described sanctions and to the entry of findings that he forged or caused to be forged a public customer's signature on a letter to his member firm requesting the issuance of a \$25,000 check. According to the findings, Cavallaro then requested that a stop payment order be placed on the check as a result of the aforesaid letter, and that a new check be issued payable to the customer. The findings also stated that Cavallaro forged or caused to be forged the customer's endorsement on the reissued check and deposited the funds in his personal bank account.

Stanley T. Conyer (Registered Representative, Lebanon, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$20,000 and barred from association with any NASD member in any capacity. Conyer was also required to pay \$98,239.96 in restitution to his member firm. Without admitting or denying the allegations, Conyer consented to the described sanctions and to the entry of findings that, without the knowledge or authorization of two public customers, he instructed his member firm to issue 12 checks totaling \$98,239.96 on the customers'

accounts, cashed the checks, and converted the proceeds to his own use and benefit.

Patrick John Crombie (Registered Representative, Columbus, Wisconsin) submitted an Offer of Settlement pursuant to which he was fined \$42,459 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Crombie consented to the described sanctions and to the entry of findings that he obtained a total of \$5,889.67 from insurance customers for the purchase of variable life insurance policies issued by his member firm. Instead of depositing the entire amount for the benefit of the customers, and without their knowledge or consent, the NASD found that Crombie deposited only \$3,430.51 with the member firm and retained the remaining \$2,459.16 for his own use and benefit.

Allen M. Denny (Registered Representative, Grand Rapids, Michigan) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$2,500 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Denny consented to the described sanctions and to the entry of findings that he received from an insurance customer a \$101.75 check with instructions to use the funds to make a payment on the customer's insurance policy. The NASD determined that Denny failed to follow the customer's instructions and used the funds for purposes other than to benefit the customer.

Charles Mark Derricotte (Registered Principal, Lorain, Ohio) and Cleveland Clifford Brooks (Registered Principal, Shaker Heights, Ohio) submitted

an Offer of Settlement pursuant to which Derricotte was fined \$7,500 and barred from association with any NASD member in any capacity. Brooks was fined \$2,500 and suspended from association with any NASD member as a general securities principal for one day. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that on separate occasions a member firm, acting through Derricotte and Brooks, failed to maintain its required minimum net capital.

The findings also stated that the same firm, acting through Brooks, made improper payment to two non-registered individuals for their efforts to secure underwritings for the firm. In addition, the NASD found that the same firm, acting through Brooks, permitted the aforementioned individuals to execute underwriting agreements on behalf of the firm.

Douglas F. Dodd (Registered Representative, Lookout Mountain, Georgia) submitted an Offer of Settlement pursuant to which he was fined \$15,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Dodd consented to the described sanctions and to the entry of findings that he recommended and executed transactions in the accounts of public customers without having reasonable grounds for believing that such recommendations and resultant transactions were suitable for the customers based on their financial situations, investment objectives, and needs. In addition, the NASD found that Dodd sent correspondence to a public customer without the prior approval of his member firm.

Thomas S. Foti (Registered

Representative, Tucson, Arizona) was fined \$5,000 and suspended from association with any NASD member in any capacity for one business day. The SEC affirmed the sanctions following an appeal of a June 1991 NBCC decision. The sanctions were based on findings that Foti caused an advertisement to be published and distributed to the public that was misleading and contained promises of specific results and exaggerated and unwarranted claims. Furthermore, Foti disseminated the advertisement without obtaining the prior written approval of a registered principal or designee of his member firm.

Richard John Hanson (Registered Representative, Edina, Minnesota) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$20,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Hanson consented to the described sanctions and to the entry of findings that he failed to respond to NASD requests for information concerning his termination from a member firm.

James C. Heffernan (Registered Representative, Alpharetta, Georgia) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Heffernan consented to the described sanction and to the entry of findings that he accepted orders for the account of a public customer from a third party who had no ownership interest in the customer's account and who had no authority to act on the customer's behalf. The findings also stated that Heffernan purchased shares of a common stock for the same customer's

account without authorization.

In addition, the NASD found that Heffernan provided another public customer with a letter guaranteeing a profit on her account, and solicited the same customer to make investments in options outside the scope of his association with a member firm.

Lynne Alstrom Hollerbach (Registered Principal, Mill Valley, California) submitted a Letter of Acceptance, Waiver and Consent pursuant to which she was fined \$43,000, barred from association with any NASD member in any capacity, and required to pay \$23,388 in restitution to a member firm.

Without admitting or denying the allegations, Hollerbach consented to the described sanctions and to the entry of findings that she obtained checks totaling \$23,388 payable to her member firm for commissions it earned on funds deposited by the firm's customers in a money market account. Instead of depositing the checks in her member firm's account, the NASD determined that without the firm's knowledge or consent, Hollerbach deposited the checks in an account that she controlled or had a beneficial interest and retained the funds for her own use and benefit. The findings also stated that Hollerbach failed to respond to NASD requests for information.

Michael S. Hughes (Registered Representative, Salt Lake City, Utah) was fined \$47,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Hughes solicited or effected securities transactions for the accounts of others and for his own account without proper registration with the SEC or the NASD.

In addition, Hughes made improper use of \$48,800 belonging to persons associated with two companies involved in a merger/acquisition and also misused 1,680,000 shares of stock belonging to the original shareholders of one of those companies by representing to them that their securities were needed to complete the merger.

Furthermore, Hughes caused misleading and unapproved sales literature recommending the purchase of stock to be disseminated to the public and failed to respond to NASD requests for information.

Kent Edward Karras (Associated Person, Chicago, Illinois) submitted an Offer of Settlement pursuant to which he was fined \$1,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Karras consented to the described sanctions and to the entry of findings that during the course of a Series 7 examination, he had in his possession notes and other materials relating to the examination despite being advised that such materials were not allowed in the examination room.

Douglas W. Kendrick (Registered Representative, Richmond, Virginia) submitted an Offer of Settlement pursuant to which he was fined \$20,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Kendrick consented to the described sanctions and to the entry of findings that he engaged in private securities transactions while failing to provide prior written notice to his member firm.

Peter K. Lloyd (Registered Representative, Odessa, Florida) was fined \$10,000, suspended from association with any NASD mem-

ber in any capacity for 20 days, and barred from association with any NASD member in any principal or supervisory capacity. The SEC affirmed the sanctions following an appeal of a March 1991 NBCC decision. The sanctions were based on findings that Lloyd sold securities to a public customer in a private securities transaction without providing his member firm with prior written notice. In addition, Lloyd made recommendations to the same customer regarding the aforementioned purchase without having reasonable grounds for believing that such recommendations were suitable based on the customer's other securities holdings and her financial situation and needs.

Jay Raymond Lovitt (Registered Representative, Shenandoah, Iowa) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000, barred from association with any NASD member in any capacity, and required to pay \$587.90 in restitution to insurance customers. Without admitting or denying the allegations, Lovitt consented to the described sanctions and to the entry of findings that, without the knowledge or consent of three customers, he received checks totaling \$587.90 intended for the purchase of insurance policies and converted the funds to his own use and benefit.

Albert M. Mikes (Registered Representative, Cleveland, Ohio) submitted an Offer of Settlement pursuant to which he was fined \$31,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Mikes consented to the described sanctions and to the entry of findings that he purchased shares of a common stock in the account of a public

customer without the customer's knowledge or consent.

Marc Lloyd Minkoff (Registered Representative, Deerfield Beach, Florida) was fined \$20,000, suspended from association with any NASD member in any capacity for 30 days, and required to requalify by examination as a general securities representative. The sanctions were based on findings that Minkoff prepared or assisted in the preparation of materially false books and records. In addition, Minkoff ordered the purchase of a low-priced security, defined by SEC Rule 15c2-6 as a designated security, for the account of a public customer without first providing the customer with a written suitability statement and without obtaining a written agreement to purchase such securities for the customer, as required by the rule.

Jonathan Garrett Ornstein (Registered Representative, Los Angeles, California) was fined \$10,000, suspended from association with any NASD member in any capacity for two years, and required to requalify by examination before acting in any registered capacity. The SEC affirmed the sanctions following an appeal of a January 1991 NBCC decision. The sanctions were based on findings that Ornstein engaged in numerous options transactions for the account of a public customer without the customer's knowledge or consent and failed to respond to NASD requests for information.

John M. Przybylinski (Registered Representative, Lombard, Illinois) submitted an Offer of Settlement pursuant to which he was fined \$42,500 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Przybylinski consented to the

described sanctions and to the entry of findings that he received from two public customers a \$2,500 check with instructions to purchase common stock. However, the findings stated that Przybylinski used the funds for purposes other than for the benefit of the customers. The findings also stated that Przybylinski failed to respond to NASD requests for information.

Karl F. Tarbox (Registered Representative, Wiscasset, Maine) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Tarbox consented to the described sanctions and to the entry of findings that he failed to pay a \$947.50 NASD arbitration award.

William G. Werling (Registered Representative, Findlay, Ohio) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$50,000, barred from association with any NASD member in any capacity, and required to pay \$14,298.78 in restitution to his member firm. Without admitting or denying the allegations, Werling consented to the described sanctions and to the entry of findings that he misappropriated and converted to his own use insurance customer funds totaling \$14,298.78. In addition, the findings stated that Werling failed adequately to respond to NASD requests for information.

Mark E. White (Registered Representative, North Little Rock, Arkansas) was fined \$5,000 and suspended from association with any NASD member in any capacity for one week. The sanctions were based on findings that White engaged in a private securi-

ties transaction with a public customer without providing prior written notification to his member firm and without obtaining prior written approval from his member firm.

Carl Everett Young, Jr. (Registered Principal, Glendale, California) was fined \$3,500, jointly and severally with a member firm, and suspended from association with any NASD member in any capacity for 30 days. The SEC affirmed the sanctions following an appeal of a November 1991 NBCC decision. The sanctions were based on findings that a member firm, acting through Young, allowed an individual to be associated with it but failed to obtain a required blanket fidelity bond to cover his activities. Further, Young engaged in a course of conduct designed to mislead the NASD staff about whether the firm had obtained a blanket fidelity bond.

Individuals Fined

Stephen Russell Boadt (Registered Principal, Pacific Palisades, California) was fined \$10,000 and ordered to requalify by examination as a financial and operations principal within 120 days or be barred in any principal capacity. The NBCC imposed the sanctions following an appeal of a District 2 DBCC decision. The sanctions were based on findings that after being ordered by the NASD in a previous disciplinary action to requalify as a financial and operations principal, Boadt continued to act in that capacity for his member firm without having so requalified.

This action has been appealed to the SEC, and the sanctions are not in effect pending consideration of the appeal.

David Kippins (Registered Representative, Brooklyn, New York) was fined \$10,000. The NBCC imposed the sanction following an appeal of a District 10 DBCC decision. The sanction was based on findings that Kippins effected transactions in the accounts of public customers without their knowledge or consent.

Donald F. Spalletta (Registered Representative, Simla, Colorado) was fined \$10,000. In the event Spalletta failed to reach an agreement to pay the arbitration award at issue within 30 days, Spalletta will be barred from association with any NASD member firm in any capacity. The NBCC imposed the sanctions following an appeal of a District 3 DBCC decision. The sanction was based on findings that Spalletta failed to pay a \$28,257.92 NYSE arbitration award.

Firms Expelled for Failure to Pay Fines and Costs in Connection With Violations

American Pacific Securities Corporation, Pasadena, California

Aristo Investments Of America, Incorporated, Miami, Florida

Clarke & Company, Villanova, Pennsylvania

Del Mar Securities, Incorporated, Del Mar, California

Southeastern Capital Group, Incorporated, Maitland, Florida

Firms Suspended

The following firms were suspended from membership in the NASD for failure to comply with formal written requests to submit financial information to the NASD. The

actions were based on the provisions of Article IV, Section 5 of the NASD Rules of Fair Practice and Article VII, Section 2 of the NASD By-Laws. The date the suspension commenced is listed after each entry. If the firm has complied with the requests for information, the listing also includes the date the suspension concluded.

BMI Financial Group, Redwood City, California (March 5, 1993)

Exchange Services, Inc., Richmond, Virginia (March 16, 1993)

First Philadelphia Corporation, New York, New York (March 5, 1993)

Fundamental Corporate Bond, New York, New York (March 19, 1993)

General Bond & Share Co., Englewood, Colorado (March 5, 1993)

Hall, Curley & Co., Inc., Norwalk, Connecticut (March 5, 1993)

McKay Investments, Inc., North Little Rock, Arkansas (March 5-24, 1993)

Pacific Inland Securities, Stockton, California (March 5, 1993)

Tierra Capital Corporation, Roswell, New Mexico (March 5, 1993)

Unex Capital Corporation, Costa Mesa, California (March 5, 1993)

Individuals Whose Registrations Were Revoked for Failure to Pay Fines and Costs in Connection With Violations

Kevin S. Allen, Carlsbad, California

Fred A. Borries, Jr., Denver, Colorado

Robert M. Celeste, Kennebunkport, Maine

Janet M. Clarke, Devon, Pennsylvania

Carolyn R. Delorraine, Boulder, Colorado

Leonard H. Dungee, Jr., Petersburg, Virginia

Joseph D. Duran, Oceanside, California

David Alan Gingras, Wallingford, Pennsylvania

Lyle R. Haas, Veradale, Washington

John A. Haralambides, Miami, Florida

Eugene Hunter, Los Angeles, California

Richard L. Larew, Ft. Lauderdale, Florida

James W. Magner, Denver, Colorado

John C. Maucere, Jr., New York, New York

Roy Smith, Jacksonville, Florida

Richard T. Wagner, Maitland, Florida

Mark A. Walloga, Brandon, Florida

FOR YOUR INFORMATION

Members Warned Against Fictitious Japanese Bond Refund Certificates

Responding to the fraudulent use of fictitious certificates called “Kanpukin Zandaka Kakuninsho,” the Japanese Ministry of Finance has issued the following warning:

- A “Kanpukin Zandaka Kakuninsho” is a fictitious certificate, allegedly issued by the Japanese Ministry of Finance, that certifies the existence of a remaining balance on a Japanese government bond refund. It claims to confirm that the Japanese Ministry of Finance will exchange the amount specified for an equivalent amount of Japanese government bonds. The Japanese government has already found several kinds of such fictitious certificates with face values ranging from 10 billion to 500 billion yen.

- Although the police have arrested some persons attempting to use these certificates, the fraudulent use of these fictitious certificates seems to have been occurring repeatedly both in Japan and overseas. The Japanese Ministry of Finance has received frequent inquiries, especially from abroad, as to whether the certificates are genuine.

- In response, the Ministry of Finance has said that it never issued such “Kanpukin Zandaka Kakuninsho,” and that such certificates are illegal.

Quarterly Press Release Now Included in *Notices to Members*

Beginning with this issue, we are now including the quarterly press release on The Nasdaq Stock MarketSM in *Notices to Members*. We hope you find the statistical information in this report useful.

SPECIAL NASD NOTICE TO MEMBERS 93-29

SEC Approves Rule 10b-6 Passive Market Making and Changes to Notification Procedures Under Schedule D of the NASD By-Laws

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The Securities and Exchange Commission (SEC) has approved an exception to SEC Rule 10b-6 (Rule 10b-6) and a new companion rule, Rule 10b-6A, under the Securities Exchange Act of 1934 to permit "passive market making" in certain distributions of securities traded on the Nasdaq National Market[®] or The Nasdaq SmallCap MarketSM during the two-business-day "cooling off" period. Currently, Rule 10b-6 generally requires market makers to withdraw from the market during the cooling-off period to prevent artificially conditioning the market to facilitate a distribution. Rule 10b-6A will permit market makers who are prospective underwriters of a distribution to remain in the market during the cooling-off period.

The NASD[®] considers adoption of passive market making to be a significant enhancement to the quality of Nasdaq[®] markets that will alleviate the negative impact of Rule 10b-6 on the cost of capital for companies involved in secondary distributions. Further, the depth and liquidity added to the market by passive market making should reduce market volatility during the cooling-off period before a secondary offering begins.

The SEC also approved amendments to Schedule D to the NASD By-Laws that require the managing underwriter of a secondary offering to inform the NASD when market makers intend to engage in passive market making under Rule 10b-6A.

The amendments to Rule 10b-6 and Rule 10b-6A become effective May 17, 1993. The text of the Schedule D amendments as well as a copy of the *Federal Register* release announcing the Rule 10b-6 changes follows this Notice.

Background

On July 27, 1992, the NASD filed an Amended Petition for Rule Making (Petition) with the SEC requesting changes to SEC Rule 10b-6 under the Securities Exchange Act of 1934 that would permit passive market making. The Petition resulted from the NASD's findings that, when compared with prices and spreads for exchange-traded securities, special liquidity problems exist in the market for Nasdaq securities during the cooling-off period before an offering. The NASD determined that these liquidity concerns arise because Nasdaq market makers must withdraw from the market to comply with Rule 10b-6. That rule prohibits persons participating in a distribution of a security and their affiliated purchasers from bidding for or purchasing, or inducing others to purchase, such security until they have completed their participation in the distribution.

On October 21, 1992, the SEC approved a release soliciting comments on the requested amendments to Rule 10b-6. The 48 comments received generally indicated strong support for the proposal. Issuers and market makers, in particular, believe that the presence of passive market making may produce a more efficient market for an issuer's securities during the cooling-off period.

Currently, an inordinate amount of volatility can occur after market makers withdraw to comply with Rule 10b-6. The NASD believes that permitting certain market makers to continue to maintain passive two-sided markets when Rule 10b-6 applies will permit market forces to operate and set the price of the security before the secondary offering without the influence of an artificially illiquid market.

Nine months following effectiveness of passive market making, the NASD will submit a report to the SEC thoroughly analyzing the amendment's operation. The SEC will then issue a release that calls for an evaluation of the effectiveness of the new rule. This release will give the NASD and market participants an opportunity to comment on the operation of passive market making.

Provisions of Passive Market Making

Security and Distribution

Qualifications — A company's securities and its prospective underwriters must meet the following requirements to be eligible for passive market making: the security must trade on the Nasdaq National Market or The Nasdaq SmallCap Market; the security must trade at no less than \$5 a share and have at least 400,000 shares in public float; and the underwriting must be a "firm commitment," fixed-price offering. Any security meeting these requirements is deemed an "eligible security."

Market makers, including both prospective underwriters and selling group members, registered in the security during the two calendar months immediately prior to the filing of the offering (reference period) are eligible to engage in passive market making. Market makers, invited to join the syndicate, must account for at least 30 percent of the average daily trading volume in the security during the two full consecutive calendar months immediately prior to the filing of the offering (30 percent Syndicate Test). This permits market makers with an extended market presence before the offering to continue providing liquidity to the market for the security. Volume data is

based on activity reported on the Nasdaq Monthly Summary of Activity Report, and passive market makers must notify the NASD of their intention to make a passive market before engaging in such activity.

Trading Restrictions Imposed on a Passive Market Maker

Passive market making is available during the two-business-day cooling-off period currently provided for in Rule 10b-6. A passive market maker's bids and purchases will be restricted based on the bidding activity of market makers registered in the security but not involved in the distribution (independent bids). Generally, for an eligible security, a passive market maker may not enter a bid or effect a purchase at a price that exceeds the highest independent bid displayed on Nasdaq. A passive market maker may engage in purchases and sales, but must close its market for the remainder of the day if its net purchases (the amount of securities purchased less sales executed) exceed 30 percent of its average daily trading volume (30 percent ADTV Limit).

Given these restrictions, a passive market maker may make a market in eligible securities, as follows:

- **Establishing the bid at the open** — at commencement of trading a passive market maker's bid cannot exceed the highest independent bid displayed for the security.
- **In a rising market** — if the best independent bid rises, a passive market maker has the option to raise its bid to match the new higher independent bid, but does not have to.
- **Restrictions in a declining market** — when the last independent bid drops below the current bid of a passive market maker(s), leaving

only passive market makers at the best inside bid, the passive market maker may maintain its higher bid until its purchases equal or exceed the "minimum exposure limit" in the Small Order Execution System (SOES)SM rules (i.e., currently 5,000, 2,500, or 1,000 shares) which the SEC defines as the "SOES mandatory exposure limit" for the security.

In its release, the SEC interprets several situations involving passive market making. Where a passive market maker, nearing its daily 30 percent ADTV Limit, has a customer sell order and a customer buy order in its possession, the passive market maker can effect both transactions with its customers contemporaneously. Therefore, though the purchase may precede the sale, the market maker would not equal or exceed its 30 percent ADTV Limit if the sale transaction is effected and reported within 90 seconds of the purchase transaction.

If a passive market maker receives a customer buy or sell order but does not have a matching order(s) to execute contemporaneous off-setting transactions against, the market maker has 15 minutes to locate a party, including another market maker, willing to take the other side of the transaction. After locating the other side of the order, the market maker must effect the first transaction then effect and report the second one within 90 seconds.

The SEC also notes that a passive market maker's ability to interact with other market makers throughout the day. They confirm that a passive market maker may hit another market maker's bid; however, the passive market maker may not take another market maker's offer.

Single-Transaction Provision, Displayed Size, and Disclosure Obligations

A passive market maker can fully execute any single order that results in the 30 percent ADTV Limit being equaled or exceeded. The passive market maker's displayed size for a security in passive market making cannot exceed the lesser of the security's SOES mandatory exposure limit or the market maker's remaining purchasing capacity under its 30 percent ADTV Limit.

The rule requires that passive market maker bids be designated as such on the Nasdaq screen. In addition, the prospectus relating to the offering of an eligible security must disclose that certain underwriters and selling group members may engage in passive market making.

* * * * *

For a complete statement and explanation of all provisions relating to passive market making see the SEC Release that follows this Notice.

Amendments to Schedule D

On April 16, 1993, the SEC also approved amendments to Schedule D that streamline the procedure for notifying the NASD when market makers intend to engage in passive market making under Rule 10b-6.

Under the streamlined procedure, the managing underwriter of the offering must notify Nasdaq Operations of the identity of not only the distribution participants but also the market makers that intend to act as passive market makers no later than 12 noon on the business day before the cooling-off period begins. The manager must advise the market makers that it has

provided such advice to Nasdaq Operations and that Nasdaq will designate their quotations as passive. Each market maker may inform Nasdaq Operations separately of its intention to act as a passive market maker or, by 4 p.m. on the business day before the cooling-off period begins, that it has decided, after the notification by the manager, not to have its quotations identified as passive.

As noted in *Notice to Members 88-69* (September 1988) the managing underwriter may employ the same streamlined procedure to inform Nasdaq Operations of those active market makers that will require an excused withdrawal when they comply with 10b-6 by ceasing market-making activities.

* * * * *

Questions regarding this Notice may be directed to Charles L. Bennett, Director, or Richard J. Fortwengler, Associate Director, NASD Corporate Financing Department at (202) 728-8258. Specific questions on the identification of market makers as passive market makers and other market-maker procedures may be directed to Nasdaq Operations at (212) 509-3618 or (800) 635-6485.

(Note: New language is underlined.)

Schedule D to the NASD By-Laws

Part VI

Requirements Applicable to Nasdaq Market Makers

* * * * *

Sec. 8. Withdrawal of Quotations and Passive Market Making

* * * * *

(d) Passive market maker status may be granted to a market maker that is a distribution participant in order to comply with Rule 10b-6 or Rule 10b-6A adopted under the Securities Exchange Act of 1934, as amended, on the following conditions:

(1) A market maker acting as a manager of a distribution may no later than noon Eastern Time on the business day prior to the beginning of the cooling-off period: (i) provide written notice to Nasdaq Operations of the contemplated date and time of the commencement of the cooling-off period, the identity of the market makers that are distribution participants that intend to act as passive market makers, and the identity of the Nasdaq security or securities subject to Rule 10b-6; and (ii) advise the market makers that they have been identified as passive market makers and that their quotations will be automatically identified as passive market maker quotations upon the request made by the manager unless they submit to Nasdaq Operations the notice specified in paragraph (2), below; provided, however, that a distribution participant shall inform Nasdaq Operations of its intention to act as a passive market maker pursuant to the procedure in subparagraph (i) if the manager does not provide the required notification.

(2) A market maker that has been identified to Nasdaq Operations as a passive market maker shall provide written notice to Nasdaq Operations and the manager of its intention not to participate in the prospective distribution or not to act as a passive market maker no later than 4:00 PM Eastern Time on the business day prior to the beginning of the cooling-off period in order to avoid having its quotations identified as the quotations of a passive

market maker.

(3) In the event the manager of a distribution is not a market maker, each market maker that is a distribution participant shall comply with Subsection (d)(1) unless another market maker has assumed responsibility for compliance.

For purposes of this paragraph (d), the term "cooling-off period" refers to the period specified in Rule 10b-6(a)(4)(xi)(A), the terms "distribution" and "distribution participant" refer to these terms as defined in Rule 10b-6(c)(5) and (c)(6), and the term "passive market maker" refers to this term as defined in Rule 10b-6A.

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 228, 229, and 240

[Release No. 33-6991, 34-32117; File No. S7-33-92]

RIN 3235-AF52

Passive Market Making

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission is adopting a new exception to Rule 10b-6 and a new companion rule, Rule 10b-6A, under the Securities Exchange Act of 1934, which permit "passive market making" by NASDAQ market makers in connection with certain distributions of NASDAQ-quoted securities during the period when Rule 10b-6 otherwise would prohibit such activity. The new

provisions apply to firm commitment distributions of NASDAQ securities that qualify for the two business day "cooling-off" period of Rule 10b-6. A passive market maker's bids and purchases are limited by the level of bids of NASDAQ market makers that are not participating in the distribution. Certain technical amendments also are being made to Rules 502 and 508 of Regulation S-B and Rules 502 and 508 of Regulation S-K under the Securities Act of 1933. The Commission will review the operation of the new rule one year following its effectiveness.

EFFECTIVE DATE: May 17, 1993.

FOR FURTHER INFORMATION CONTACT:

Nancy J. Sanow, M. Blair Corkran, Elizabeth Pucciarelli Hensley, or Susan H. Schleisner, Office of Trading Practices, Division of Market Regulation, at (202) 272-2848, Securities and Exchange Commission, 450 Fifth Street, NW., Mail Stop 5-1, Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

I. Introduction

The Securities and Exchange Commission ("Commission") is adopting a new exception to Rule 10b-6¹ and a companion rule, Rule 10b-6A, under the Securities Exchange Act of 1934 ("Exchange Act"),² which permit "passive market making" on the National Association of Securities Dealers Inc.'s ("NASD") Automated Quotation system ("NASDAQ") during the period when Rule 10b-6 otherwise would prohibit such activity.

The Commission proposed the passive market making provisions in response to an amended petition for rulemaking filed with the Commission by the NASD in July 1992.³ The passive market making proposal reflected a cooperative effort between the Commission and the NASD to permit a market presence by NASDAQ market makers when they or their "affiliated purchasers"⁴ are engaged in a

¹ 17 CFR 240.10b-6.

² 15 U.S.C. 78(a) *et seq.*

³ See Securities Exchange Act Release No. 31347 (October 22, 1992), 52 FR 49039 ("Proposing Release").

The NASD filed a petition for rulemaking, and an amendment thereto ("NASD Petition"), with the Commission requesting that it amend Rule 10b-6 to permit "passive market making" during certain distributions. The NASD filed the original petition on June 28, 1991, pursuant to Section 553(e) of the Administrative Procedure Act, 5 U.S.C. 553(e), and Rule 4(a) of the Commission's Rules of Practice, 17 CFR 201.4(a). The original submission, supplementary material, and the July 27, 1992 amendment are available in the Commission's Public Reference Section at the address noted above in File No. S7-33-92.

⁴ "Affiliated purchaser" is defined in 17 CFR 240.10b-6(c)(6).

distribution for Rule 10b-6 purposes, subject to certain conditions designed to maintain the Rule's anti-manipulation objectives.

Forty-eight comment letters were received in response to the Proposing Release.⁵ Forty-six commenters supported the passive market making proposal. Generally, these commenters stated that the new rule would enhance market depth and liquidity during the covered period. Twenty-one commenters suggested various modifications to the proposal. While not expressly supporting or opposing the proposal, two commenters, both of which are national securities exchanges, stated that analogous relief from the provisions of Rule 10b-6 for exchange specialists affiliated with distribution participants should be granted.

The Commission has determined to adopt the passive market making proposal with several modifications suggested by commenters. Rule 10b-6A reduces the restrictions on the market activities of broker-dealers participating in certain distributions of NASDAQ securities and thus should facilitate capital formation by NASDAQ issuers. The Commission expects the NASD, at the end of a nine month period following effectiveness of the new rule, to submit a report thoroughly analyzing the operation of Rule 10b-6A and the adequacy of its surveillance procedures governing passive market making activity. Shortly thereafter, the Commission will issue for public comment a report evaluating the effectiveness of the rule. The Commission believes that this time frame will be sufficient for the NASD and the Commission to obtain information on the operation of passive market making and make any changes, if needed, to the rule. Because the rule introduces a new construct to permit distribution participants to continue market making activities during the Rule 10b-6 cooling-off period, it may function in unanticipated ways and require adjustments prior to the end of the review period. In that event, the Commission would consider making appropriate "mid-course" adjustments prior to the expiration of this period.⁶

⁵ The Commission received letters from 29 NASDAQ issuers, nine broker-dealers, four associations, four self-regulatory organizations, and two law firms. A Summary of Comments has been prepared by the Division of Market Regulation ("Division") and is included in File S7-33-92. The Summary of Comments does not include one comment letter received from a broker-dealer after the Summary was prepared.

⁶ The Division is conducting a general review of the operation of Rule 10b-6 and related provisions. The results of this review also may affect the Commission's evaluation of passive market making.

II. Background

Rule 10b-6 is an anti-manipulation rule that is intended to prevent participants in a distribution of securities from artificially conditioning the market for the securities in order to facilitate the distribution, and to protect the integrity of the securities trading market as an independent pricing mechanism. Rule 10b-6 applies to securities offerings that present a potential for manipulation, and covers those persons who may have an incentive to manipulate the market during the distribution. Adopted in 1955, Rule 10b-6 codifies "principles which historically have been applied in considering questions relating to manipulative activity and stabilization in connection with a distribution."⁷ Specifically, Rule 10b-6 prohibits persons⁸ participating in a distribution⁹ of a security and their affiliated purchasers from bidding for or purchasing, or inducing others to purchase, such security or any related security¹⁰ until they have completed their participation in the distribution.¹¹

Rule 10b-6 contains several exceptions to its general prohibitions that are intended to permit an orderly distribution of securities or to limit disruptions in the market for the securities being distributed. In particular, paragraph (a)(4)(xi)¹² of Rule 10b-6 ("Exception (xi)") allows an underwriter, prospective underwriter, or dealer, or their affiliated purchasers, among other things, to effect solicited principal transactions¹³ prior to a two

or nine business day "cooling-off" period. This exception reflects the desirability of maintaining depth and liquidity in the market for the issuer's securities consistent with the anti-manipulation objectives of the Rule.¹⁴ Once the cooling-off period commences, the distribution participant and its affiliated purchasers must suspend solicited principal activities, including market making (unless otherwise excepted by Rule 10b-6), until the termination of the distribution.¹⁵

As described more fully in the NASD Petition and the Proposing Release, the NASD believes that special liquidity problems exist in the NASDAQ market during the cooling-off period prior to an offering, relative to prices and spreads for exchange-traded securities. The NASD Petition ascribes these liquidity concerns to the withdrawal from the market of NASDAQ market makers that must comply with the provisions of Rule 10b-6 when they or their affiliated purchasers participate in a distribution. Therefore, the NASD requested that the Commission amend Rule 10b-6 to permit a NASDAQ market maker to engage in passive market making transactions in NASDAQ securities designated as national market system ("NMS") securities and that qualify for the two business day cooling-off period.

III. The New Exception and Rule

New paragraph (a)(4)(xiv) to Rule 10b-6 excepts passive market making transactions effected in compliance with Rule 10b-6A from the general prohibitions of Rule 10b-6.

A. Eligibility Requirements

1. Securities

As proposed, to be eligible for passive market making a security would have had to: (1) Be a NASDAQ/NMS security;¹⁶ (2) have a minimum price of five dollars per share and a minimum public float of 400,000 shares, as computed in accordance with Rule 10b-6(c)(7) ("\$/400,000 Share Test");¹⁷ and

(3) have NASDAQ market makers who are underwriters or prospective underwriters,¹⁸ or affiliated purchasers of underwriters or prospective underwriters, that, in the aggregate, account for at least 40 percent of the average daily trading volume ("ADTV")¹⁹ in the security ("syndicate ADTV"), during the two full consecutive calendar months immediately preceding the date of filing of the registration statement under the Securities Act pertaining to the eligible security to be distributed ("reference period"). The purpose behind the \$5/400,000 Share Test and the NASDAQ/NMS condition was to require that eligible securities have markets of sufficient depth and liquidity and be subject to real-time transaction reporting that would facilitate surveillance to detect manipulative activity.

The Commission received comments on all of the above three eligibility requirements. Several commenters supported eliminating the requirement that eligible securities be designated as NMS securities, on the basis that the \$5/400,000 Share Test suffices to identify liquid securities, and that NASDAQ Small-Cap securities (i.e., non-NMS NASDAQ securities) also are subject to real-time reporting requirements.²⁰ In response to the comments, the rule, as adopted, allows any NASDAQ security satisfying the \$5/400,000 Share Test to be eligible for passive market making.²¹

subject of the distribution, or any related security, until two business days prior to the commencement of offers or sales of the securities to be distributed. 17 CFR 240.10b-6(a)(4)(xi)(A).

In order to be eligible for passive market making, a "related security" as defined in Rule 10b-6A(b)(12) must satisfy the eligibility criteria set forth in this section. See n.10 *supra*.

¹⁸ These terms are defined in 17 CFR 240.10b-6(c)(1) and (2).

¹⁹ The ADTV constitutes the daily trading volume in an eligible security as reported to the NASD by the market maker and thereafter reported by the NASD in a monthly report ("NASD Monthly Activity Report").

²⁰ All securities quoted on NASDAQ are now subject to real-time transaction reporting. In 1992, Schedule D to the NASD By-Laws was amended to add requirements for trade reporting for securities quoted on the "NASDAQ Small-Cap Market" that are similar to the trade reporting requirements for NASDAQ/NMS securities. NASDAQ Small-Cap securities are not reported pursuant to Section 11A under the Exchange Act, 15 U.S.C. 78k-1, and are not NMS securities. See Securities Exchange Act Release No. 30569 (April 10, 1992), 57 FR 13396.

²¹ In response to the Commission's request for comment, eight commenters addressed the issue of whether a security eligibility standard based on the dollar value of ADTV is more indicative of market depth and liquidity and should be used in place of the \$5/400,000 Share Test. Five commenters favored keeping the \$5/400,000 Share Test on the basis that it is easy to apply and has worked well in the context of Rule 10b-6. Three commenters, however, urged revisions to this test and suggested

Continued

⁷ Securities Exchange Act Release No. 5040 (May 18, 1954), 19 FR at 2986. See also IX L. Loss & J. Seligman, Securities Regulation 4015 (3d ed. 1992).

⁸ Among others, Rule 10b-6 applies to issuers, underwriters, prospective underwriters, dealers, brokers, and other persons who have agreed to participate or are participating in a distribution. With particular reference to the NASD Petition, the Rule covers market makers when they or their affiliated purchasers are involved in a distribution.

⁹ "Distribution" is defined in 17 CFR 240.10b-6(c)(5) as an offering of securities, whether or not subject to registration under the Securities Act of 1933 ("Securities Act"), 15 U.S.C. 77a *et seq.*, that is distinguished from ordinary trading transactions by the magnitude of the offering and the presence of special selling efforts and selling methods.

¹⁰ "Related security" refers to: (A) A security of the same class and series or right to purchase the security in distribution; or (B) a security that is deemed to be in distribution because of the operation of Rule 10b-6(b), 17 CFR 240.10b-6(b), which provides that the distribution of a security (1) which is immediately exchangeable for or convertible into another security, or (2) which entitles the holder thereof immediately to acquire another security, shall be deemed to include a distribution of such other security within the meaning of Rule 10b-6. See Rule 10b-6A(b)(12).

¹¹ See Securities Exchange Act Release No. 19565 (March 4, 1983), 48 FR 10628 ("Release 34-19565").

¹² 17 CFR 240.10b-6(a)(4)(xi).

¹³ The publication of a market maker's bid quotation involves a solicitation for the security.

¹⁴ See Securities Exchange Act Release No. 24003 (January 16, 1987), 52 FR 2994.

¹⁵ See 17 CFR 240.10b-6(c)(3). Any transactions effected in accordance with any of the exceptions to Rule 10b-6, including exception (a)(4)(xi), may not be engaged in for the purpose of creating actual, or apparent, active trading in or raising the price of the covered securities. 17 CFR 240.10b-6(a)(4).

¹⁶ NASDAQ/NMS securities are securities that are: quoted on NASDAQ; and subject to real-time reporting pursuant to a transaction reporting plan filed by the NASD under Section 11A of the Exchange Act, 15 U.S.C. 78k-1. See also Schedule D of the NASD By-Laws, Part XIII, NASD Manual (CCH) ¶¶ 1867A-1867C.

¹⁷ 17 CFR 240.10b-6(c)(7). The criteria included those contained in paragraph (a)(4)(xi)(A) of Rule 10b-6, which permit distribution participants to solicit purchases of the securities that are the

The Commission requested that commenters consider whether the 40 percent syndicate criterion was appropriate, or should be raised or lowered, and whether it would affect syndicate formation. One commenter believed that a level higher than 40 percent would be appropriate. Ten commenters, however, indicated that the Commission should delete or reduce the 40 percent syndicate criterion on the basis that a level as high as 40 percent may affect syndicate formation because the managing underwriter may invite market makers into the syndicate solely to reach the 40 percent threshold. One commenter opposing the 40 percent criterion, stated that a market maker accounting for a percentage of ADTV substantially lower than that level still could represent the principal and most important source of liquidity in the market for that security.

In response to commenters, the Commission has determined to modify this provision in the final rule, while retaining its essential function.²² As adopted, NASDAQ market makers who are underwriters or prospective underwriters or affiliated purchasers of underwriters or prospective underwriters must, in the aggregate, account for at least 30 percent of the ADTV in the security during the reference period ("30% Syndicate Test").²³ This lower level responds to commenters' suggestions that a reduced level may be more appropriate, because it may help relieve pressure to expand

alternative standards, such as an ADTV of at least \$500,000 for the security; reliance on factors such as market capitalization, number of institutional holders, dollar value of ADTV, the number of market makers; and dollar value of public float. One commenter stated that the \$5/400,000 Share Test was inappropriate because of the susceptibility of small companies' stocks to price manipulation, and suggested limiting the availability of the passive market making provisions to issuers with a minimum market capitalization of \$200 million. Following a comprehensive review of Rule 10b-6 and related provisions, the Commission may determine to modify Rule 10b-6's current standard for reliance on the two business day cooling-off period, and thus revise the corresponding criterion for passive market making eligibility.

²² One commenter recommended that a market maker be given flexibility in calculating its own ADTV level, suggesting, for example, a "rolling" 60 day standard. The staff of the Division will consider specific no-action requests from individual firms that wish to calculate their own ADTV over some period other than the two calendar month period provided for in Rule 10b-6A. Such individual requests should be submitted to the Division, along with appropriate information on the basis for the alternative ADTV calculation. The firm concurrently should notify the NASD that it is making such a request.

²³ The NASD will calculate and provide to the managing underwriter the ADTV levels for prospective market makers for purposes of the 30% Syndicate Test and the net purchase limitation discussed *infra* in Section III.C.

the syndicate to reach the required level.

The Commission believes that the adopted 30% Syndicate Test is consistent with its belief that passive market making be available only in those instances when Rule 10b-6 otherwise would require a withdrawal of substantial market making capacity. This determination also is consistent with the rationale underlying the NASD Petition: passive market making should be allowed where the market for NASDAQ securities is affected adversely when market makers otherwise are required to withdraw their quotations.

2. Distributions

The Commission has adopted the requirement that passive market making be limited to distributions of securities registered pursuant to the Securities Act and underwritten on a firm commitment basis at a fixed price. One commenter urged modifying this condition to accommodate non-registered and at-the-market offerings. Since the application of Rule 10b-6A to non-registered and at-the-market offerings would be complex and the NASD's surveillance plan would not easily accommodate such offerings, this provision is adopted as proposed.

3. Qualifying Period

As adopted, passive market making is permitted from the time an eligible market maker otherwise would be prohibited from effecting transactions in an eligible security under the terms of Rule 10b-6(a)(4)(xi)(A) (the two business day cooling-off period), until the earlier of the time of the commencement of offers or sales in the distribution or the time at which a stabilizing bid in such security is made pursuant to Rule 10b-7²⁴ under the Exchange Act ("qualifying period"). Although this period typically will be two business days, it may be longer (for example, if the scheduled effective date of the registration statement is delayed) or shorter (for example, if pre-effective stabilization is undertaken). This provision is adopted as proposed.

4. Market Makers

As proposed, to be eligible to engage in passive market making, Rule 10b-6A

²⁴ 17 CFR 240.10b-7. Rule 10b-7 governs the placing of stabilizing bids or the effecting of stabilizing purchases to facilitate an offering. Stabilization does not encompass transactions that raise the price of the security or create actual, or apparent, active trading greater than that necessary to prevent or retard a decline in the price. The Commission has observed that similarities of purpose and effect exist between stabilization and passive market making. See Release 34-19565.

required a market maker to be registered on NASDAQ in the securities that are the subject of the distribution: (1) during the reference period;²⁵ and (2) during the qualifying period. Under the proposal, NASDAQ market makers who are distribution participants (including a member of the selling group who is not an underwriter or prospective underwriter) satisfying the above requirements would have been permitted to engage in passive market making.

Several commenters addressed the requirement conditioning eligibility for passive market making on NASDAQ registration in the offered security during the reference period. Some favored a one-month reference period; another commenter favored eliminating the requirement because it appeared to preclude broker-dealers who were not market makers for the entire two-month reference period from engaging in passive market making.

After considering the comments received, the Commission has determined to delete the proposed reference period and qualifying period requirements in paragraph (b)(9) of the proposed rule. Broker-dealers are not precluded from engaging in passive market making because they were not registered as NASDAQ market makers at the beginning of the reference period or were not so registered for the entire period. However, as adopted, Rule 10b-6A will continue to limit a passive market maker's purchases to 30 percent of its ADTV,²⁶ which will be provided by the NASD on the basis of NASDAQ market making transactions effected during the reference period.²⁷ Accordingly, a broker-dealer that was a NASDAQ market maker for only a portion of the reference period would have a proportionately reduced ADTV because the volume is averaged over the total number of trading days during that two-month period.²⁸ The qualifying period requirement has been deleted as superfluous, because by the rule's definition a broker-dealer must be registered as a NASDAQ market maker

²⁵ As stated above, the reference period is the two calendar months immediately preceding the filing of the registration statement in connection with the offering. Rule 10b-6A(b)(11).

²⁶ See Section III.C. *infra*.

²⁷ See n.23 *supra* and accompanying text.

²⁸ Trading days in which a market maker does not effect any trades in the eligible security will reflect a trading volume of zero for purposes of calculating the ADTV. In calculating a market maker's ADTV, the NASD will not consider days on which the market maker has obtained an excused withdrawal pursuant to NASD rules. See Section 8 of Schedule D to the NASD By-Laws. NASD Manual (CCH) ¶ 1824.

in order to engage in passive market making.²⁹

B. Level of Market Maker Bids

As adopted, during the qualifying period, Rule 10b-6A prohibits a passive market maker generally from entering a bid or effecting a purchase in an eligible security at a price that exceeds the highest bid for those securities displayed on NASDAQ by a market maker that is not participating in the distribution and is not an affiliated purchaser³⁰ of a distribution participant ("independent bid").³¹ Rule 10b-6A does not require that a passive market maker's bid equal other passive market makers' bids.

If all independent bids for an eligible security are lowered below a passive market maker's bid made in accordance with Rule 10b-6A, a passive market maker may continue to effect purchases at its bid at a price exceeding the then-highest independent bid until the passive market maker's purchases (aggregate, not net) equal or exceed an amount equal to the mandatory exposure limit in the NASD's small order execution system ("SOES")³² ("SOES mandatory exposure limit")³³

²⁹ See Rule 10b-6A(c)(1).

³⁰ The term "affiliated purchaser" includes "a person directly or indirectly acting in concert" with a distribution participant in the acquisition or distribution of the distribution security or any related security. 17 CFR 240.10b-6(c)(6)(i)(A). For example, if a distribution participant influenced an ostensibly independent market maker to publish a bid or make purchases at some price or at certain times, the market maker would be an affiliated purchaser, and its bids and purchases could not be used to determine the permissible levels of passive market making activity. In addition, such activity likely would violate Rule 10b-6. See, e.g., *SEC v. Scott Taylor & Co., Inc.*, 183 F. Supp. 904, 908 (S.D.N.Y. 1959).

³¹ In the event that no independent bid exists in the market (i.e., all market makers in a security are members of the syndicate), then passive market making would not be permitted.

³² SOES was designed to provide the benefits of immediate execution to retail customer orders for securities quoted on NASDAQ by permitting orders to be executed automatically at the best bid or ask price ("inside market"). SOES is restricted to public customer orders of 1,000 or fewer shares in NASDAQ/NMS securities and 500 or fewer shares in NASDAQ non-NMS securities. See Securities Exchange Act Release No. 29809 (October 10, 1991), 56 FR 52092.

³³ The SOES mandatory exposure limit is the number of shares of a security that a market maker is required to accept for its account through SOES executions. Specifically, the SOES mandatory exposure limit for a security is the aggregate number of shares of the security equal to five times the maximum order size for that security. The term maximum order size means the maximum size of individual orders for a security that may be entered into or executed through SOES. All NASDAQ/NMS securities are in one of three tiers of maximum order sizes in SOES: 1,000, 500, and 200. See NASD Rules of Practice and Procedures for the Small Order Execution System, Sections a-f, NASD Manual (CCH) ¶¶ 2451-2470.

for the security.³⁴ Once the passive market maker has purchased an amount equal to the SOES mandatory exposure limit, the passive market maker must immediately lower its bid to a level not higher than the highest independent bid. In addition, a passive market maker may purchase all of the securities that are part of any *single* order that, when executed, results in the SOES mandatory exposure limit being equalled or exceeded without having to withdraw its quotations.³⁵ These provisions facilitate the execution of customer orders by allowing the passive market maker to remain in the market, and give passive market makers an opportunity to remain at their bid during a short-term lowering of the bids of independent market makers.

One commenter supported, and two commenters opposed, the general requirement that a passive market maker's bids must follow independent bids. The latter commenters argued that the passive market makers would possess the most knowledge about the issuer and its business and, therefore, should be relied upon to maintain and protect the security's trading market and pricing mechanism. In the Commission's view, the condition governing permissible levels of market maker bids is the very essence of passive market making. It reflects the Commission's effort to reconcile the goal of Rule 10b-6 (i.e., preventing price-influencing activity by distribution participants, who have an incentive to condition the market for securities in distribution) with the desirability of adding liquidity to the NASDAQ market during periods when distribution participants otherwise would be prohibited from making markets.

C. Purchase Limitation

As proposed, on each business day³⁶ of the qualifying period, a passive

³⁴ This purchasing provision is not limited to SOES transactions. All passive market making purchases would count against the permitted SOES mandatory exposure limit level. A passive market maker's purchases also are restricted by its net purchase limit.

³⁵ A market maker who sought to combine two or more orders to purchase an amount of shares that it would not be able to purchase if the transactions were executed separately would not be within the provisions of Rule 10b-6A. The Commission expects that the NASD will monitor carefully those transactions that take a market maker over the SOES mandatory exposure limit for the security to ensure that orders are not aggregated to take advantage of this provision.

³⁶ Consistent with Rule 10b-6, the staff interprets a business day as a twenty-four hour period determined with reference to the principal market for the security, and that includes a complete trading session for that market (i.e., the same-day opening and closing on NASDAQ). See Letter

market maker's net purchases³⁷ in an eligible security could not have exceeded 25 percent of its ADTV in that security during the reference period. Several commenters opposed the proposed 25 percent ADTV level for various reasons, including difficulty of compliance, lack of necessity in light of the independent bid requirement, lack of purchasing limits in the context of passive market making in foreign markets³⁸ and Rule 10b-7 stabilization activities. Others suggested increasing the ADTV limit, with one commenter suggesting 40 percent on the basis that it would achieve a better balance in promoting a two-sided market, and would lend itself to greater uniformity in light of the proposed 40 percent syndicate criterion for market maker eligibility.

The Commission is adopting the provision subjecting each passive market maker to a daily net purchase limitation. The proposed 25 percent ADTV level, however, is being increased to a level of 30 percent ("30% ADTV Limit").³⁹ The Commission believes that the 30 percent level responds to commenters' suggestions that the purchasing volume limitation be raised.

The ADTV will be derived from the NASD Monthly Activity Report, and will be provided by the NASD to market makers. Based on this information, each passive market maker will be required to determine its 30% ADTV Limit. When a passive market maker's net

regarding Rule 10b-6: Interpretation of "Business Day" (July 29, 1991), [1991] Fed. Sec. L. Rep. (CCH) ¶ 79,751.

³⁷ "Net purchases" are defined as the amount by which a passive market maker's purchases exceeds its sales. See Rule 10b-6A(b)(8).

³⁸ See, e.g., Letter regarding the International Stock Exchange of the United Kingdom and the Republic of Ireland Limited (now the London Stock Exchange ("LSE")) (September 29, 1987), [1987] Fed. Sec. L. Rep. (CCH) ¶ 78,713, as modified in Letter regarding the International Stock Exchange of the United Kingdom and the Republic of Ireland Limited (October 14, 1988) [available on LEXIS], and Letter regarding Distribution of Certain SEAQ Securities (December 1, 1992) [available on LEXIS] (exemptions from Rules 10b-6 and 10b-7 to permit LSE market makers to engage in a form of passive market making transactions on the Stock Exchange Automated Quotations system during the period that the provisions of Rule 10b-6 normally would prohibit such activities).

³⁹ The Commission believes that it is desirable to give passive market makers flexibility regarding the treatment of SOES volume in connection with passive market making activities. Therefore, a passive market maker may opt to exclude SOES volume from its passive market making activities, see *supra* n.33 and accompanying text. In other words, a passive market maker may disregard SOES purchases when calculating its net purchases. If the market maker elects this option, it must disregard SOES sales in determining its purchasing capacity. If a passive market maker excludes SOES volume from its 30% ADTV Limit, then SOES volume also must be excluded in determining the market maker's ADTV during the reference period.

purchases equal or exceed its 30% ADTV Limit at any time during the qualifying period. Rule 10b-6A requires the passive market maker to withdraw its quotations from NASDAQ immediately, and prohibits the passive market maker from effecting any transactions for the remainder of that day unless otherwise permitted by Rule 10b-6.⁴⁰

The Commission believes that the net purchasing provision reflected in the 30% ADTV Limit appropriately permits passive market makers to contribute significantly to market liquidity, while it limits the potential for price impact through such activities. A price limit alone would not prevent market makers from influencing the security's price. Even where a market maker's bids and purchases do not lead the market, they can stimulate activity by others at higher levels and can support prices at higher levels.⁴¹ The Commission also believes that an average daily trading limit based on net purchases, rather than aggregate purchases, recognizes that the price impact of market maker sales may tend to offset the effects of market maker purchases. It is also important to note that, with a net purchasing provision, passive market makers will be able to continue to provide liquidity throughout the qualifying period where their trading position is relatively "flat," which is typical of normal market making.

With regard to comments concerning the complexity of a net purchase formulation, the Commission believes that NASDAQ market makers tend to monitor closely their trading positions, and particularly will do such monitoring when they are involved in underwritings. Moreover, they have the capability (enhanced by automated systems) to determine if the 30% ADTV Limit has been exceeded. Once NASDAQ market makers become familiar with passive market making, concerns about its complexity should ease.

As proposed, a passive market maker's aggregate purchases during the last full hour of trading on NASDAQ that precedes the pricing of the eligible security to be distributed could not have exceeded an amount equal to the proposed 25 percent ADTV level

⁴⁰ A market maker whose net purchases on Day 1 of the qualifying period are less than its 30% ADTV Limit cannot carry over the balance to Day 2. A passive market maker that has withdrawn its quotations from the market cannot re-enter passive market making quotations during that day irrespective of other transactions that it may effect pursuant to other Rule 10b-6 exceptions.

⁴¹ See, e.g., *SEC v. Scott Taylor & Co., Inc.*, 183 F. Supp. 904, 908 (S.D.N.Y. 1959); *Halsey, Stuart & Co., Inc.*, 30 S.E.C. 106, 121 (1949).

reduced by the passive market maker's net purchases as of the beginning of that hour ("last-hour provision").

Several commenters opposed the last-hour provision on the grounds that it was unnecessary and too complicated, and also impractical because of the difficulty in determining the exact time of the offering's pricing. The NASD argued that, because the hour prior to pricing is critical to the efficient pricing of the offering, a restriction on a passive market maker's ability to commit capital during this hour would increase the security's volatility.

The Commission has determined not to adopt any special limitation on purchases during the last hour of trading prior to pricing. Accordingly, a passive market maker's purchases during the last hour will be subject to the same 30% ADTV Limit that is applicable during the rest of the day.

The proposed last-hour provision was based upon a concern that passive market makers could effect sales earlier in the day with a view to entering the last hour with the ability to purchase a very large amount of shares that would in effect stabilize the price of the security. It is not clear, however, that such a strategy would be viable, given the likely impact of those sales. Moreover, the Commission agrees with commenters who argued that a special last-hour provision would have added complexity to the rule. The Commission expects, however, that the NASD will monitor passive market making activity during the final trading hour prior to pricing closely, and provide the Commission with data on last hour transactions. The Commission will consider that information in determining whether the rule should be revised to include a special last hour limitation when the rule is reviewed following the monitoring period.

As adopted, Rule 10b-6A permits a passive market maker to complete any single order that, when executed, equals or exceeds its 30% ADTV Limit.⁴² Immediately after executing the order, the market maker must withdraw its quotations from NASDAQ. Once a passive market maker has withdrawn its bid, it may not enter any bids for, nor effect any purchases of, the eligible security for the remainder of that day irrespective of additional sales, absent the applicability of a separate exception to Rule 10b-6.

⁴² The NASD has represented that it will monitor carefully those transactions that are permissible but take a market maker over its 30% ADTV Limit to ensure that there is no aggregation of orders to take advantage of this exception or other inappropriate activity.

D. Passive Market Making Interpretations

The provisions described above are designed to reflect the fundamental premise underlying passive market making: Bidding and purchasing activity is to be passive, *i.e.*, bids limited by the prices of independent market makers, and purchases limited by such prices and effected in response to order flow. This section discusses interpretations that are intended to reflect this premise. These interpretations, which were included in the Proposing Release, have been modified in response to the comments received.

1. Interaction With Other Market Makers

The Proposing Release stated that:

[I]f a passive market maker has a net sales position during the day, it may not affirmatively take another market maker's offer to reduce its short position. Conversely, if the passive market maker is in a net purchase position, it may not affirmatively hit another market maker's bid to reduce its long position. The passive market maker may only adjust its quotations within the parameters of [the proposed rule] to solicit transactions on one side of the market or the other.⁴³

This statement was intended as an explication of what "passive" activity encompassed. In fact, since a passive market maker cannot make a bid or purchase above the level of the highest independent bid, and the highest bid will be below the lowest offer (except in unusual circumstances), the statement that a passive market maker could not take another market maker's offer (*i.e.*, make a purchase) did not constitute a limitation not already included in the passive market making concept.

In general, however, neither Rule 10b-6 nor Rule 10b-6A is concerned with sales activity. The Commission agrees, therefore, with commenters who pointed out that it is not necessary to restrict sales even in instances where a passive market maker initiates the transaction with another market maker. For example, a passive market maker may affirmatively hit another market maker's bid to reduce a long position. This has been reflected in Rule 10b-6A(c), which applies passive market making conditions only to "transactions," which is defined in paragraph (b)(15) as "bids or purchases."

⁴³ Proposing Release, 52 FR at 49047, n.87. The "contemporaneous customer transaction" and the "15 minute provision" discussed below deal with situations that the Commission believes will occur rarely during the qualifying period, but may provide useful guidance to passive market makers

2. Contemporaneous Customer Transaction

Where a market maker has in its possession both a customer order to sell and a customer order to purchase an eligible security, the passive market maker may effect the transactions as principal with each customer contemporaneously. In this situation, the sequence in which the transactions are executed would be ignored so long as the second transaction is effected and reported within 90 seconds of the execution of the first transaction,⁴⁴ and only the net position would be relevant to passive market making activity. For example, if the purchase from one customer (passive market maker purchase) occurs before the sale to the other customer and the sale is effected and reported within 90 seconds of the execution of the first transaction, then the market maker will not be deemed to have equalled or exceeded its 30% ADTV Limit. No comments were received on this interpretation.

3. 15 Minute Provision

In the event a market maker receives a customer sell or customer buy order and the market maker does not have in its possession a matching order or orders with which contemporaneous offsetting executions can be effected,⁴⁵ the market maker is permitted to hold the initial order for a time period not to exceed 15 minutes, in which time the market maker can attempt to locate a party, other than another market maker, willing to take the other side of the transaction. In this limited situation,⁴⁶ the Commission does not consider the market maker's efforts to locate the matching order⁴⁷ to be proscribed solicited activity.⁴⁸ If the market maker locates customer interest for the other side of the order in the appropriate time frame, the market maker must effect the

transactions contemporaneously as described in Section III.D.2. above (*i.e.*, the second transaction must be effected and reported within 90 seconds of the execution of the first transaction).

Several commenters opposed the 15 minute provision, while several others suggested modifications. One commenter suggested that the time limit should relate to the security's ADTV, so that market makers would have more time to locate the other side of an order in a security with a lower ADTV and less time in an actively-traded security. Others believed that the passive market maker should be able to match the order with an unsolicited order of another market maker. One commenter stated that, if, at the end of the 15 minute period the order is still unmatched, the market maker should be able to "hit" another market maker's bid.

The Commission believes that the 15 minute provision provides flexibility for passive market makers while at the same time it prevents a passive market maker from improperly withholding a sell order from the market for an extended period or executing a customer purchase order in a manner that would vitiate the efficacy of the passive market making conditions. Consistent with the discussion above of sales activity by passive market makers and the suggestion of a commenter, during the 15 minute period a passive market maker could "hit" other market makers' bids to fill the customer sell order.

Finally, given the limited nature of the activities discussed in these interpretations, the Commission has determined not to include the interpretations in the text of Rule 10b-6A.

E. Limitation on Displayed Size

As adopted, Rule 10b-6A requires that, at all times, each passive market maker's displayed size may not exceed the SOES mandatory exposure limit⁴⁹ for the eligible security, or its remaining purchasing capacity as set forth in Section III.C. above, whichever is smaller. The Commission has determined to adopt this provision as proposed.

F. Disclosure of Passive Market Making

Because passive market making represents a significant change in the level of distribution participant activity in the market, and bears some resemblance to stabilization activity, the Commission believes that disclosure of

passive market making is necessary and appropriate to inform the market of its potential impact on the price and volume of eligible securities.

1. Bid Disclosure

Rule 10b-6A, as adopted, requires that the bid displayed by a passive market maker be designated as such.⁵⁰ This identification will alert investors and other market participants that distribution participants are effecting passive market making transactions, and will facilitate surveillance of their activities. Each passive market maker is responsible for confirming that its passive market making bids are identified properly. One comment supporting this provision was received.

2. Prospectus Disclosure

The Commission has determined to require that the following legend be included on the inside front cover of the prospectus for any offering in which any passive market maker intends to enter bids or effect purchases in any eligible security:

In connection with this offering, certain underwriters (and selling group members) or their affiliates may engage in passive market making transactions in (identify each class of securities in which such transactions may be effected) on NASDAQ in accordance with Rule 10b-6A under the Securities Exchange Act of 1934. See "Plan of Distribution."

The Commission has revised the language to accommodate commenters' concerns that the legend as proposed appeared to require information that would not be known at the time the preliminary prospectus is filed. This legend disclosure requirement is being adopted as an amendment to Rule 502(d)⁵¹ of Regulation S-K under the Securities Act rather than as a part of Rule 10b-6A. This should facilitate compliance by preparers of prospectuses. Similarly, the Commission is adopting, as an amendment to Rule 508⁵² of Regulation S-K under the Securities Act, the requirement that the prospectus contain a brief description of passive market making in the "Plan of Distribution" section. Similar amendments have been made to Rules 502(d)⁵³ and 508⁵⁴ of Regulation S-B under the Securities Act.

⁵⁰ NASDAQ operations will insert a special designation next to the quotations of a passive market maker.

⁵¹ 17 CFR 229.502(d).

⁵² 17 CFR 229.508.

⁵³ 17 CFR 228.502(d).

⁵⁴ 17 CFR 228.508.

⁴⁴ NASDAQ market makers are required to report a transaction within 90 seconds of its execution. Schedule D of the NASD By-laws, Part XII, Section 2. NASD Manual (CCH) ¶ 1867. Therefore, the execution of the first transaction by the market maker will start the 90 second "clock," and the market maker will be required to report that trade, and execute and report the second trade, within the 90 second period in order for them to be considered contemporaneous.

⁴⁵ See Section III.D.2.

⁴⁶ This would be the situation where the passive market maker received a customer order during the qualifying period that exceeded the size of the passive market maker's quotation and that the passive market maker did not wish to execute because it would cause it to exceed its 30% ADTV Limit, although such a transaction is permitted under the rule (see text at n.42 *supra*).

⁴⁷ Except as described in Section III.D.1. above, the passive market maker cannot fill the order with other market makers.

⁴⁸ The market maker's solicitation activities are limited to only those necessary to offset the order.

⁴⁹ As discussed in n.33 *supra*, the SOES mandatory exposure limit for a security is the aggregate number of shares of the security equal to five times the maximum order size for that security.

3. Transaction Disclosure

Paragraph (c)(10) of the proposed rule would have required a passive market maker who sells to, or purchases any eligible security for the account of, any person to give or send to such person, at or before the completion of each transaction, written notice that passive market making transactions may be or have been effected. If, however, at or before the completion of the transaction, the purchaser received a prospectus, confirmation, or other writing containing disclosure similar to that described in Section III.F.2., then no other written notice would have been required to be given to such purchaser.⁵⁵

Commenters argued that investors would not find transaction notice of passive market making meaningful and that, in light of prospectus disclosure, separate transaction notice would be unnecessary. One commenter pointed out that investors currently do not receive notification when market makers have to withdraw from the market in accordance with the provisions of Rule 10b-6. The Commission has decided not to require transaction disclosure for investors who purchase securities that are the subject of passive market making. When the Commission revisits Rule 10b-6A, it may reconsider whether transaction disclosure should be required.

G. Notice and Reporting to the NASD

As adopted, Rule 10b-6A requires a market maker to provide advance written notification to the NASD of its intention to engage in passive market making. The notice must include information demonstrating that the security, distribution, and market maker qualify for passive market making.⁵⁶ In addition, the new rule requires that a passive market maker submit to the NASD information about passive market making purchases, in such form as the NASD shall prescribe.

Three commenters provided their views on the proposed notice and reporting requirements. One commenter considered the requirements unnecessary; another remarked that while these requirements may be appropriate, there is no mechanism to enforce compliance; and a third stated that the new rule should list the types

of information to be submitted to the NASD.

The Commission has determined to adopt the notice and reporting requirements as proposed. The notice will ensure that the NASD's Surveillance Department receives adequate and timely notification of market makers' intentions to engage in passive market making and thus can initiate the appropriate surveillance procedures to monitor the market for the security that is the subject of the distribution. The NASD is in a better position to determine the specific information that will permit it to conduct appropriate surveillance. Also, the information submitted to the NASD will be useful in the preparation of the NASD's findings and analysis of the operation of passive market making.

H. Transactions at Prices Resulting From Unlawful Activity

As adopted, paragraph (d) provides that no bids or purchases of an eligible security may be made at a price that the passive market maker knows or has reason to know is the result of activity that is fraudulent, manipulative, or deceptive under the Exchange Act or any rule or regulation thereunder.⁵⁷ Furthermore, any transactions by a passive market maker engaged in for the purpose of creating actual, or apparent, active trading in or raising the price of an eligible security will not be within the provisions of exception (a)(4)(xiv), which incorporates Rule 10b-6A.⁵⁸

I. Surveillance Procedures

The NASD has developed a comprehensive surveillance plan for passive market making that includes on-line monitoring and a review and analysis of historical quotation and trading information, as well as the use of the NASD's existing automated surveillance reports. The Commission considers the surveillance plan to be a critical element of the passive market making concept, and expects to work with the NASD during the pilot period to refine and monitor the surveillance procedures.

J. Rule Review

The Commission has determined to adopt Rule 10b-6A as a final rule, but views the rule to be operational on a pilot basis. The Commission expects the NASD to monitor carefully all instances of passive market making to determine its impact on the NASDAQ market during the nine month period following

the effectiveness of Rule 10b-6A, and shortly thereafter to provide the Commission with a report about the rule's operation during the nine month period. The Commission believes it would be appropriate, after some experience is gained with the operation of the new rule and the NASD has submitted sufficient data, to evaluate its operation. The Commission, therefore, directs the Division of Market Regulation to prepare a report evaluating the effectiveness of the rule. The report will be issued within 90 days after the rule has been fully operative for nine months, and will be issued for public comment. Once interested parties have commented, and the Commission has made its own evaluation, the Commission will decide what, if any, revisions are appropriate.

IV. Final Regulatory Flexibility Analysis

A final regulatory flexibility analysis has been prepared regarding the amendments to Rule 10b-6 and the adoption of Rule 10b-6A in accordance with 5 U.S.C. 604. A copy of the analysis may be obtained by contacting K. Susan Grafton, Division of Market Regulation, 450 Fifth Street, NW., Washington, DC 20549.

V. Effects on Competition

Section 23(a) of the Exchange Act⁵⁹ requires the Commission, in adopting rules under the Exchange Act, to consider the anti-competitive effects of such rules, if any, and to balance any impact against the regulatory benefits gained in terms of furthering the purposes of the Exchange Act. In the Proposing Release, the Commission solicited commenters' views on whether the proposed rule would result in any anti-competitive impact, particularly as the proposed exception is applicable to a single United States market. Two exchanges submitted comments requesting that the Commission simultaneously promulgate a rule that would permit specialists affiliated with distribution participants to continue to make markets during the cooling-off periods of Rule 10b-6. In particular, the New York Stock Exchange, Inc. ("NYSE"), noting that passive market making does not apply to the NYSE's market structure and its specialist system, proposed that a specialist organization that is an affiliated purchaser of a distribution participant and that has obtained exemptive relief pursuant to NYSE Rule 98⁶⁰ be entitled

⁵⁵ This proposed provision was modeled upon the transaction disclosure requirement in connection with stabilization activities. See Proposing Release, 57 FR at 49046.

⁵⁶ Cf. Schedule D to the NASD By-laws, Part VI, Section 3, NASD Manual (CCH) ¶ 1820 (requiring market makers to provide advance notice to the NASD of their intention to engage in stabilization).

⁵⁷ Cf. 17 CFR 240.10b-7(f).

⁵⁸ See Rule 10b-6(a)(4). Moreover, the general antifraud and anti-manipulation provisions of the securities laws continue to apply.

⁵⁹ 15 U.S.C. 78w(a)(2).

⁶⁰ Rule 98, Restrictions on Approved Persons Associated with a Specialist's Member

to a total exemption from Rule 10b-6 under certain specified conditions. These conditions would be premised on a specialist meeting its market making obligations, the existence of effective transaction monitoring by the specialist, and effective specialist surveillance by the NYSE. In contrast, two commenters stated that it was unnecessary to provide relief to exchange specialists.

The Commission has determined that exception (a)(4)(xiv) of Rule 10b-6 and Rule 10b-6A, as adopted, will not impose any significant burden on competition not necessary or appropriate in furtherance of the Exchange Act. Transactions on an exchange are not affected by the pendency of a distribution in the way that over-the-counter transactions are. The principal market makers in a NASDAQ security often will be chosen by the issuer as underwriters for the distribution. Rule 10b-6 requires such market makers to withdraw from the market at the commencement of the cooling-off period unless an exception is available. Such withdrawal can affect the depth and liquidity for the security, and the 30% Syndicate Test is designed to limit passive market making to those situations where these effects are likely to be significant. In contrast, exchange specialists do not participate in distributions. Rule 10b-6 requires the specialist to suspend its specialist activities, however, when an affiliate is a distribution participant. In such situations, exchange rules provide for a transfer of the specialist "book,"⁶¹ and the continuation of specialist functions.

The limitations on market making activity contained in Rule 10b-6A are not compatible with the obligations imposed on specialists to maintain orderly markets,⁶² and the exchanges have not suggested that passive market making would work in that context. Instead, the exchanges have suggested a different construct for Rule 10b-6 relief for specialists. The Commission recognizes that "passing the book" causes some degree of disruption to specialist activity, and exemptions from Rule 10b-6 have been granted in

appropriate circumstances.⁶³ As part of the Commission's ongoing review of Rule 10b-6, its staff is evaluating the appropriateness of broader relief for exchange specialists.

VI. Statutory Basis and Text of Rule Amendments

Rule 10b-6A and the amendments to Rule 10b-6 are adopted under the Exchange Act, 15 U.S.C. 78a *et seq.*, and particularly Sections 2, 3, 9(a)(6), 10(a), 10(b), 15(c)(2), and 23(a) of the Exchange Act, 15 U.S.C. 78b, 78c, 78i(a)(6), 78j(a), 78j(b), 78o(c)(2), and 78w(a). The amendments to Items 502 and 508 of subpart 228.500 and Items 502 and 508 of subpart 229.500 are adopted under the Securities Act, 15 U.S.C. 77 *et seq.*

List of Subjects in 17 CFR Parts 228, 229, and 240

Broker-dealers, Fraud, Issuers, Reporting and recordkeeping requirements, Securities.

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 228—INTEGRATED DISCLOSURE SYSTEM FOR SMALL BUSINESS ISSUERS

1. The authority citation for part 228 continues to read as follows:

Authority: 15 U.S.C. 77e, 77f, 77g, 77h, 77j, 77k, 77s, 77aa(25), 77aa(26), 77ddd, 77eee, 77ggg, 77hhh, 77jjj, 77nnn, 77sss, 78l, 78m, 78n, 78o, 78w, 78ll, 80a-8, 80a-29, 80a-30, 80a-37, 80b-11, unless otherwise noted.

2. In § 228.502 paragraph (d) is redesignated as follows:

Old paragraph	New paragraph
(d) heading	(d)(1)
(d)(1)	(d)(1)(i)
(d)(2)	(d)(1)(ii)
(d)(3) introductory text.	(d)(1)(iii) introductory text
(d)(3) (i) through (v).	(d)(1)(iii) (A) through (E)

3. Section 228.502 is further amended by adding new paragraph (d)(2) as follows:

§ 228.502 (Item 502) Inside front and outside back cover pages of prospectus.

- (d)(1) *Stabilization.* * * *
- (2) *Passive market making.* Include the following statement, if true:

⁶¹ See, e.g., Letter regarding Application of Rules 10b-6 and 10b-13 to Specialists Affiliated with NYSE Member Firms (September 15, 1992) [1992] Fed. Sec. L. Rep. (CCH) ¶ 76,279.

IN CONNECTION WITH THIS OFFERING, CERTAIN UNDERWRITERS [AND SELLING GROUP MEMBERS] MAY ENGAGE IN PASSIVE MARKET MAKING TRANSACTIONS IN THE [IDENTIFY EACH CLASS OF SECURITIES IN WHICH SUCH TRANSACTIONS MAY BE EFFECTED] ON NASDAQ IN ACCORDANCE WITH RULE 10b-6A UNDER THE SECURITIES EXCHANGE ACT OF 1934. SEE "PLAN OF DISTRIBUTION."

4. Section 228.508 is amended by adding paragraph (i) to read as follows:

§ 228.508 (Item 508) Plan of distribution.

(i) *Passive market making.* If the underwriters or any selling group members intend to engage in passive market making transactions as permitted by § 240.10b-6A of this chapter, indicate such intention and briefly describe passive market making.

PART 229—STANDARD INSTRUCTIONS FOR FILING FORMS UNDER SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934 AND ENERGY POLICY AND CONSERVATION ACT OF 1975—REGULATION S-K

5. The general authority citation for part 229 continues to read in part as follows:

Authority: 15 U.S.C. 77e, 77f, 77g, 77h, 77j, 77k, 77s, 77aa(25), 77aa(26), 77ddd, 77eee, 77ggg, 77hhh, 77iii, 77jjj, 77nnn, 77sss, 78c, 78i, 78j, 78l, 78m, 78n, 78o, 78w, 78ll(d), 79e, 79n, 79t, 80a-8, 80a-29, 80a-30, 80a-37, 80b-11, unless otherwise noted.

6. In § 229.502 paragraph (d) is redesignated as follows:

Old paragraph	New paragraph
(d) heading	(d)(1)
(d)(1)	(d)(1)(i)
(d)(2)	(d)(1)(ii)
(d)(3) introductory text	(d)(1)(iii) introductory text
(d)(3)(i) through (v) ...	(d)(1)(iii)(A) through (E)

7. Section 229.502 is further amended by adding new paragraph (d)(2) as follows:

§ 229.502 (Item 502) Inside front and outside back cover.

Pages of Prospectus

- (d)(1) *Stabilization.* * * *
- (2) *Passive Market Making.* If the registrant or any of the underwriters

Organization, NYSE Guide (CCH) ¶ 2098. Rule 98 provides relief for entities in a control relationship with a specialist organization from other NYSE rule restrictions that otherwise would be applicable to such entities' transactions in securities in which the specialist organization is registered, or to business transactions with the issuers of such securities.

⁶¹ See NYSE Rules 104.15, 104.17, 106A, and 460.20, NYSE Guide (CCH) ¶¶ 2104.15, 2104.17, 2106A, and 2460.20; Amex Rules 172 and 173, Amex Guide (CCH) ¶¶ 9312 and 9313.

⁶² See NYSE Rule 104, NYSE Guide (CCH) ¶ 2104; Amex Rule 170, Amex Guide (CCH) ¶ 9310.

knows or has reason to believe that there is an intention to engage in passive market making transactions in compliance with § 240.10b-6A of this chapter, set forth a statement in substantially the following form, subject to appropriate modification where circumstances require. Such statement shall be in capital letters, printed in boldface roman type at least as large as ten-point modern type and at least two points leaded:

IN CONNECTION WITH THIS OFFERING, CERTAIN UNDERWRITERS [AND SELLING GROUP MEMBERS] MAY ENGAGE IN PASSIVE MARKET MAKING TRANSACTIONS IN THE [IDENTIFY EACH CLASS OF SECURITIES IN WHICH SUCH TRANSACTIONS MAY BE EFFECTED] ON NASDAQ IN ACCORDANCE WITH RULE 10b-6A UNDER THE SECURITIES EXCHANGE ACT OF 1934. SEE "PLAN OF DISTRIBUTION."

* * * * *

8. Section 229.508 is amended by adding paragraph (k) to read as follows:

§ 229.508 (Item 508) Plan of distribution.

* * * * *

(k) *Passive market making.* If the underwriters or any selling group members intend to engage in passive market making transactions as permitted by § 240.10b-6A of this chapter, indicate such intention and briefly describe passive market making.

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

9. The authority citation for part 240 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78i, 78j, 78l, 78m, 78n, 78o, 78p, 78s, 78w, 78x, 78j(d), 79q, 79t, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4 and 80b-11, unless otherwise noted.

* * * * *

10. Section 240.10b-6 is amended by removing the "." at the end of paragraph (a)(4)(xiii) and replacing it with a "; or" and adding paragraph (a)(4)(xiv) to read as follows:

§ 240.10b-6 Prohibitions against trading by persons interested in a distribution.

(a) * * *

(4) * * *

(xiv) Market making transactions complying with § 240.10b-6A.

* * * * *

11. Section 240.10b-6A is added to read as follows:

§ 240.10b-6A Passive market making.

(a) *Scope of section.* This section permits broker-dealers to engage in market making transactions in eligible securities without being in violation of the provisions of § 240.10b-6.

(b) *Definitions.* Unless the context otherwise requires, all terms used in this section shall have the same meaning as in the Act and § 240.10b-6 thereunder. In addition, unless the context otherwise requires, the following definitions shall apply:

(1) The term *ADTV* means the average daily trading volume in an eligible security during the reference period, as obtained from the NASD. If a passive market maker excludes SOES volume from the calculation of its net purchases as defined in paragraph (b)(8) of this section, then SOES volume also must be excluded in determining the market maker's ADTV.

(2) The term *30% ADTV Limit* means 30 percent of the market maker's ADTV.

(3) The term *eligible security* means a NASDAQ security that:

- (i) Is the subject of a firm commitment, fixed price offering registered under the Securities Act of 1933 or is a related security;
- (ii) Has a minimum price of five dollars per share and a minimum public float of 400,000 shares, as computed in accordance with § 240.10b-6(c)(7); and
- (iii) Has NASDAQ market makers that are underwriters or prospective underwriters, or affiliated purchasers of underwriters or prospective underwriters, that account for at least 30% of the total trading volume in such security, as reported to the NASD for the reference period.

(4) The term *independent bid* means a bid for a security displayed on NASDAQ by a market maker who is not participating in the distribution of that security or a related security, and is not an affiliated purchaser of such a participating market maker.

(5) The term *NASD* means the National Association of Securities Dealers, Inc.

(6) The term *NASDAQ* means the NASDAQ system as defined in § 240.11Ac1-2(a)(3).

(7) The term *NASDAQ security* means a security that is authorized for quotation on NASDAQ, and such authorization is not suspended, terminated, or prohibited.

(8) The term *net purchases* means the amount by which a passive market maker's purchases exceed its sales. A passive market maker's SOES purchases and sales may be excluded from the calculation of net purchases if the adjustments to ADTV are made as

required by paragraph (b)(1) of this section.

(9) The term *passive market maker* means a market maker that effects transactions in accordance with the provisions of paragraph (c) of this section.

(10) The term *qualifying period* means the period from the time that a passive market maker would otherwise be prohibited from effecting transactions in an eligible security under the terms of § 240.10b-6(a)(4)(xi)(A), until the earlier of the time of commencement of offers or sales of the eligible security to be distributed or the time at which a stabilizing bid for such security is made pursuant to § 240.10b-7.

(11) The term *reference period* means the two full consecutive calendar months immediately preceding the date of filing of the registration statement under the Securities Act of 1933 pertaining to the security to be distributed.

(12) The term *related security* means:

- (i) A security of the same class and series as, or a right to purchase, the security to be distributed or deemed to be in distribution; and
- (ii) Any security deemed to be in distribution pursuant to § 240.10b-6(b).

(13) The term *SOES* means the NASD's Small Order Execution System, as defined in the NASD Rules of Practice and Procedures for the Small Order Execution System.

(14) The term *SOES mandatory exposure limit* means the aggregate number of shares of the security equal to five times the maximum order size for that security that may be entered into or executed through SOES.

(15) The term *transaction* means a bid or a purchase.

(c) *Conditions to be met.*

(1) *General limitations.* A passive market maker must effect all transactions in the capacity of a registered market maker on NASDAQ. Except as provided below, during the qualifying period, a passive market maker shall not effect a transaction in an eligible security at a price that exceeds the highest independent bid for the eligible security at the time of the transaction.

(2) *Level of bid.* A passive market maker may display its bid at a price not in excess of the highest independent bid for an eligible security.

(3) *Requirements to lower the bid.* If all independent bids for an eligible security are lowered below the passive market maker's bid, the passive market maker must lower its bid to a level not higher than the then highest independent bid; *Except That:*

(i) The passive market maker may continue to effect purchases at its bid at a price exceeding the then highest independent bid until the passive market maker purchases an amount of the eligible security that equals or exceeds the SOES mandatory exposure limit for that security; and

(ii) A passive market maker may purchase all of the securities that are part of a single order that, when executed, results in the SOES mandatory exposure limit being equalled or exceeded.

(4) *Purchase limitation.* On each day of the qualifying period, a passive market maker's net purchases shall not exceed its 30% ADTV Limit; *Except* That a passive market maker may purchase all of the securities that are part of a single order that, when executed, results in its 30% ADTV Limit being equalled or exceeded. If a passive market maker's net purchases equal or exceed its 30% ADTV Limit, it shall immediately withdraw its quotations from NASDAQ, and it may not effect any transaction in the eligible security for the remainder of that day, irrespective of any additional sales during that day, unless otherwise permitted by § 240.10b-6.

(5) *Limitation on displayed size.* At all times, the passive market maker's displayed bid size may not exceed the smaller of the SOES mandatory exposure limit for the eligible security, or the passive market maker's remaining purchasing capacity under paragraph (c)(4) of this section.

(6) *Identification of a passive market making bid.* The bid displayed by a passive market maker shall be designated as such.

(7) *Notification and reporting to the NASD.* A passive market maker shall notify the NASD in writing in advance of its intention to engage in passive market making. A passive market maker shall submit to the NASD information regarding passive market making purchases in such form as the NASD shall prescribe.

(8) *Prospectus disclosure.* The prospectus for any offering in which any passive market maker intends to effect transactions in any eligible security shall contain the information required in §§ 228.502, 228.508, 229.502 and 229.508 of this chapter.

(d) *Transactions at prices resulting from unlawful activity.* No transaction shall be made at a price which the passive market maker knows or has reason to know is the result of activity which is fraudulent, manipulative, or deceptive under the Act or any rule or regulation thereunder.

Dated: April 8, 1993

By the Commission.
Margaret H. McFarland,
Deputy Secretary.
[FR Doc. 93-8710 Filed 4-14-93; 8:45 am]
BILLING CODE 8010-01-P

NASD NOTICE TO MEMBERS 93-30

NASD Provides SEC- Approved Clarifications and Interpretations to Recent Net Capital Rule Amendments

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On November 24, 1992, the Securities and Exchange Commission (SEC) adopted significant amendments to the Net Capital Rule, Rule 15c3-1. The changes to the minimum net capital requirements will take effect in three installments beginning July 1, 1993; other changes took effect on January 1. Additional amendments to the rule, published for comment in December, are still being considered. This Notice sets forth, in question and answer format, certain guidelines for compliance with the new requirements.

Background

As announced in *Notice to Members 92-72* (December 15, 1992), several amendments to the SEC's Net Capital Rule were effective January 1. One change concerning market makers is effective July 1, 1993. The net capital ceiling for a market maker will increase to \$1 million as of that date. The changes to the rule's minimum net capital requirements will take effect in three steps starting July 1, 1993.

The adopted amendments increase the required minimum net capital for firms that carry customer accounts to at least \$250,000 (\$100,000 for those firms that operate pursuant to the paragraph (k)(2)(i) exemption of Rule 15c3-3); create two classes of introducing firms each with a different minimum requirement (at least \$50,000 for firms that receive but do not hold customer securities for deliv-

ery to the clearing broker/dealer

and \$5,000 for firms that do not receive customer funds or securities); increase the minimum to at least \$100,000 for dealers and underwriters that trade solely for their own accounts; increase the minimum to at least \$25,000 for firms that transact a business in mutual fund shares and certain other share accounts on other than a subscription-way basis; increase the minimum requirements for market makers to at least \$100,000; and maintain a \$5,000 minimum category for other broker/dealers that do not handle customer funds or securities.

Other adopted amendments establish one standardized method of calculating haircuts for all firms; adopt the alternative method for computing concentration charges for all firms; reduce the impact on aggregate indebtedness for two items (mutual funds payable offset by fails to deliver and corresponding stock loan/stock borrow); and permit the use of an offset when computing the open contractual commitment haircut on underwritings.

Since publication of *Notice to Members 92-72*, several NASD members have raised questions concerning the new requirements. The Association is publishing the answers to certain of these questions for the benefit of all members.

Questions concerning this Notice may be directed to Samuel Luque, Associate Director, Financial Responsibility at (202) 728-8472.

Minimum Net Capital Quick Reference Guide

	<u>Minimum Dollar Requirements</u>	<u>Phase-in Periods</u>		
	Amended to	July 1, 1993	Jan. 1, 1994	July 1, 1994
Mutual fund dealers subscription basis	5,000	3,300	4,100	5,000
Mutual fund dealers wire-order basis	25,000	10,000	17,500	25,000
*Introducing firms not receiving funds/securities	5,000	5,000	5,000	5,000
Introducing firms receiving securities	50,000	20,000	35,000	50,000
Firms carrying customer accounts under k(2)(i) exempt/15c3-3	100,000	50,000	75,000	100,000
Dealers and market makers	100,000	50,000	75,000	100,000
*Brokers' brokers	150,000	150,000	150,000	150,000
Firms carrying customer accounts basic (AI) method	250,000	100,000	175,000	250,000
Firms electing the alternative method	250,000	150,000	200,000	250,000
**Futures commission merchants	250,000	250,000	250,000	250,000
*Other brokers or dealers	5,000	5,000	5,000	5,000

Note: Whenever a broker/dealer engages in more than one of the above activities the highest requirement for any of those activities is the dollar requirement.

Ratio requirements and other requirements for futures commission merchants and market makers may dictate requirements higher than the minimum dollar requirement.

* Denotes no change.

** Futures Commission Merchant = National Futures Association minimum.

Item

SEC Net Capital Rule

Minimum Net Capital Requirements

I. Firms That Carry Accounts:

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------|
| A. Firms that carry customer accounts or broker or dealer accounts and receive or hold funds or securities for those persons | |
| i. Basic Method | Greater of \$250,000 or 6 2/3% of AI |
| ii. Alternative Method | Greater of \$250,000 or 2% of Rule 15c3-3 Reserve Formula debits |
| B. Firms that carry customer accounts, receive but do not hold customer funds or securities, and operate under the paragraph (k)(2)(i) exemption of Rule 15c3-3 | Greater of \$100,000 or 6 2/3% of AI |

II. Introducing Brokers:

- | | |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------|
| A. Firms that introduce accounts on a fully disclosed basis to another broker or dealer and do not receive funds or securities | Greater of \$5,000 or 6 2/3% of AI |
| B. Firms that introduce accounts on a fully disclosed basis to another broker or dealer and receive, but do not hold, customer or other broker/dealer securities and do not receive funds | Greater of \$50,000 or 6 2/3% of AI |

III. Dealers

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------|
| Brokers or dealers that trade solely for their own accounts, endorse or write options, or effect more than ten transactions for their investment account in any one calendar year | Greater of \$100,000 or 6 2/3% of AI |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------|

Item (cont.)

SEC Net Capital Rule (cont.)

IV. Mutual Fund Brokers or Dealers

Brokers or dealers transacting a business in redeemable shares of registered investment companies and certain other share accounts

- | | |
|---------------------------------------------------------------------------------|-------------------------------------|
| A. Wire orders | Greater of \$25,000 or 6 2/3% of AI |
| B. Application method, and do not otherwise receive or hold funds or securities | Greater of \$5,000 or 6 2/3% of AI |

V. Market Makers

A broker or dealer engaged in activities as a market maker

Greater of \$100,000 or 6 2/3% of AI or \$2,500 per security for securities with a market value greater than \$5 per share, and \$1,000 per security for securities with a market value of \$5 or less with a maximum requirement of \$1 million

VI. Other Broker or Dealers

- | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------|
| A. Firms that deal only in Direct Participation Programs (DPPs) | Greater of \$5,000 or 6 2/3% of AI |
| B. Firms that do not take customer orders, hold customer funds or securities, or execute customer trades, because of the nature of their activities (e.g., mergers and acquisitions) | Greater of \$5,000 or 6 2/3% of AI |

VII. Alternative Method

Any firm may elect this method, however, they will be subject to the \$250,000 minimum net capital requirement

Greater of \$250,000 or 2% of Rule 15c3-3 Reserve Formula debits

Item (cont.)

SEC Net Capital Rule (cont.)

VIII. Securities Haircuts

- | | |
|------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------|
| A. Equity securities | 15% of the market value of the greater of the long or short position, plus 15% of the lesser to the extent it exceeds 25% of the greater position |
| B. Undue concentration | The charge for undue concentration for equities is 15%, applied to the concentrated position immediately |

IX. Aggregate Indebtedness

- | | |
|----------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------|
| A. Mutual funds payable offset to fails to deliver | 85% of the amounts payable related to fails to deliver of the same quantity and issue of registered investment company shares is excluded from AI |
| B. Stock loan and stock borrowed | 85% of stock loan payables related to stock borrowed receivables of the same class and issue is excluded from AI |

X. Contractual Charges

- | | |
|--------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| A. Open contractual commitment haircut for securities designated as Nasdaq National Market® or listed on a national securities exchange | 15% haircut |
| B. Open contractual commitment haircut for securities not designated as Nasdaq National Market or listed on a national securities exchange | 30% haircut; however, for brokers or dealers with more than \$250,000 in net capital, the first \$150,000 of the haircut need not be deducted in the computation of net capital |

XI. Secured Demand Note Collateral

- | | |
|--------------------------------------------------------------------------|-------------|
| Other securities including equities collateralizing secured demand notes | 30% haircut |
|--------------------------------------------------------------------------|-------------|

Questions and Answers Relating to the Amendments to the Uniform Net Capital Rule

Question #1: Should a fully disclosed introducing firm (current \$5,000 minimum requirement), that does *not* have a clearing agreement stating that the introduced customer accounts are the responsibility of the carrying firm, be considered self-clearing (with a \$25,000 current minimum requirement) immediately?

Answer: No. By June 30, 1993, introducing firms will be required to have properly executed clearing agreements stating that introduced customer accounts are the responsibility of the carrying firm. If a proper clearing agreement is not executed, an introducing firm can no longer be considered an introducing firm. Such a firm will have a minimum net capital requirement of \$250,000.

Question #2: If a customer disregards written instructions (i.e., the confirmation) to make the check payable to the clearing broker/dealer and submits a check to the introducing broker/dealer, made payable to the introducing firm, will the introducing broker/dealer's requirement increase from \$5,000 to \$250,000?

Answer: No. The SEC has recognized that on occasion customers will mistakenly make their checks payable to the introducing firm. However, the burden of demonstrating mistakes rests with the introducing firm. Firms must have procedures in place to demonstrate how such customer mistakes will be addressed. The confirmation should always indicate that checks are to be made payable to the clearing firm, escrow agent, or appropriate third party. Customers making such mistakes should be contacted

directly, in writing, and instructed regarding the proper procedures.

Question #3: Into which net capital category does an introducing firm that receives and promptly transmits customer checks made out to third parties fall?

Answer: An introducing firm that receives and promptly transmits all customer and broker/dealer checks made payable to the appropriate third party will have a minimum requirement of \$5,000, provided that the firm does not receive customer securities.

Question #4: In *Notice to Members 92-72*, it was noted that the adopted amendments created two classes of introducing firms. However, some firms introduce accounts on a fully disclosed basis and separately transact business in mutual fund shares through a (k)(2)(i) "Special Bank Account." Since the firm is *receiving* funds from customers for its mutual fund business, is the firm's minimum net capital requirement \$250,000?

Answer: No. An introducing firm that processes customer monies related to its mutual fund business through a (k)(2)(i) account will be required to maintain net capital of not less than \$25,000, provided that other activities of the firm do not require a higher net capital.

Question #5: If an introducing broker/dealer receives checks payable to itself, deposits the checks in a (k)(2)(i) account, and then promptly forwards the funds to its clearing broker/dealer, would the introducing broker/dealer be subject to a minimum net capital requirement of \$100,000 or \$250,000?

Answer: The firm would be deemed to have received customer funds if it operates in this manner

and, therefore, would be subject to the \$250,000 minimum net capital requirement. The SEC has informed us that a (k)(2)(i) account cannot be used by fully disclosed firms, except for mutual fund transactions.

Question #6: Can a \$5,000 firm accept customers' funds and forward such funds to its clearing firm? If so, under what circumstances?

Answer: Yes. If the checks are made payable to the clearing firm and promptly forwarded.

Question #7: What would be the minimum net capital requirement for an introducing firm that trades for its own account, makes no markets, and does not participate in firm commitment underwritings?

Answer: An introducing firm that effects more than 10 transactions in its investment account during a calendar year will be required to maintain \$100,000 in net capital. (Transactions in money market instruments are excluded from the 10-transaction limitation.) If 10 or fewer transactions are effected, the minimum net capital requirement would be either \$5,000 or \$50,000, as appropriate for introducing firms. (A transaction is either a purchase or sale.)

Question #8: Is an introducing broker/dealer, that has the ability to *write* checks or drafts on the clearing broker/dealer's behalf, subject to a higher net capital requirement than the \$5,000 required for an introducing broker/dealer?

Answer: No. If the bank account is in the name of the clearing firm, and there is a written contract between the carrying broker/dealer and the introducing firm specifying that the introducing firm is acting as agent for the carrying broker/dealer,

the introducing firm's minimum net capital requirement will be \$5,000.

Question #9: What is an introducing broker/dealer's net capital requirement, if it receives checks from a mutual fund made payable to the firm with a reference to the customer's name and account number? (The checks are the customer's dividends and capital gains, which the customer wants deposited in its brokerage account and the customer has requested that the mutual fund send the checks to the broker/dealer.)

Answer: A firm that receives checks from a mutual fund made payable to itself, resulting from dividends or capital gains in a customer's account, will have a net capital requirement of \$250,000. The fact that the customer requested this transaction would not alter this requirement.

Question #10: Does the required clearing agreement for introducing firms (i.e., the agreement must state that customers are the customers of the clearing firm for purposes of the Securities Investors Protection Act, that account statements must be sent directly to customers, etc.) apply to a \$5,000 introducing firm as well as to a \$50,000 introducing firm?

Answer: Yes. All fully disclosed introducing firms will be required to execute clearing agreements that contain the appropriate language as outlined in *Notice to Members 92-72* (see page 517). The language required by the Rule to be included in all clearing agreements is intended to establish the concept that the customers must look to the clearing firm for the payment of monies and delivery of securities.

Question #11: If a firm (i) conducts a general securities business

on a fully disclosed basis, receives no customer securities, and all customer checks are made payable, and promptly forwarded, to the clearing firm, and (ii) deposits customer checks made payable to itself for mutual fund transactions (only) into a (k)(2)(i) "Special Bank Account" and promptly transmits the firm's own check to the mutual fund issuer, what would be the broker/dealer's net capital requirement?

Answer: Based on its mutual fund wire-order business, the firm's net capital requirement would be \$25,000, and the firm would claim the (k)(2)(i) exemption from the Customer Protection Rule.

Question #12: If a sole mutual fund dealer (current \$2,500 minimum requirement) receives checks made payable to the fund, what will its new capital requirement be?

Answer: A firm that operates pursuant to 15c3-1(a)(2)(v), acting only on a subscription-order basis with respect to the purchase and sale of open-end mutual fund shares and insurance company separate accounts, and receives checks made payable to the appropriate third party, will have a minimum net capital requirement of \$5,000.

Question #13: What is the net capital requirement for a firm that acts as the underwriter for a mutual fund?

Answer: A broker/dealer that engages solely in mutual fund transactions will be required to maintain a minimum net capital of \$5,000, provided that all trades are done on a subscription basis directly with the fund. The requirement for a firm that conducts a similar business but on a wire-order basis will be \$25,000.

Question #14: What is the minimum net capital requirement for a firm that holds mutual fund securities in street name on behalf of customers?

Answer: The requirement is \$250,000, the same as for any firm that holds securities on behalf of its customers, regardless of whether the securities are mutual fund shares, equities, or debentures.

Question #15: Does the \$1,000 per security requirement for market makers go into effect on July 1, 1993, the same time that the \$1 million ceiling goes into effect?

Answer: No. The requirement to maintain net capital of not less than \$1,000 per security with a market value of \$5 or less for those securities in which they make a market became effective on January 1, 1993. The current \$100,000 ceiling requirement will be increased to \$1 million effective July 1, 1993.

Question #16: Does a broker/dealer calculating net capital under the alternative standard require SEC approval if it wishes to change to the aggregate indebtedness standard?

Answer: Yes. Also, any firm that wishes to compute net capital under the alternative standard after January 1, 1993, must file the appropriate notification with its Designated Examining Authority. If the firm wishes to change from the alternative standard, it must obtain prior approval from the SEC before the change can be made.

Question #17: What is the contractual charge for initial public offerings and secondary offerings listed on the Nasdaq National Market or an exchange?

Answer: For all securities being

underwritten in an initial public offering, the percentage deduction applied as the open contractual commitment charge is 30 percent, even if the issue immediately begins trading in the secondary market on the Nasdaq National Market or an exchange. If the underwriting is a secondary offering of an issue already trading on the Nasdaq National Market or an exchange, the percentage is 15 percent.

Question #18: What is the open contractual commitment charge for a firm commitment underwriting of a new convertible debt security that is immediately convertible into an existing Nasdaq National Market security for the same issuer?

Answer: The open contractual commitment charge for a convertible debt security is calculated by multiplying the dollar amount of the commitment by the appropriate percentage as determined by Rule 15c3-1 (c)(2)(vi)(G). If the security has a market value at par or higher, the percentage deduction is determined by Rule 15c3-1(c)(2)(vi)(J). If the security has a market value less than par, the percentage deduction is determined by Rule 15c3-1(c)(2)(vi)(F).

Question #19: What is the new net capital requirement for a direct participation program firm that does not have a (k)(2)(i) account and does not “receive” customer funds?

Answer: A firm, which limits its activities to selling direct participation programs or other similar securities and uses an escrow account pursuant to SEC Rule 15c2-4, will be in the \$5,000 minimum net capital category and will not be required to have a (k)(2)(i) account.

Question #20: Is a sole government securities firm going to be

subject to any changes in liquid capital requirements?

Answer: No. At this time, the adopted amendments to the Net Capital Rule will not change the liquid capital requirements for a sole government securities firm.

Question #21: Should a NASD-designated member firm increase its fidelity bond in six-month intervals as the minimum net capital requirements increase, or may the firm wait until it is time to renew the bond?

Answer: Article III, Section 32, requires a member firm to review annually the adequacy of its fidelity bond coverage. This review is required annually at the anniversary date of the issuance of the bond.

Question #22: Will a new member be subject to the new minimum requirements immediately, or will it be subject to the temporary phase-in minimums allowed existing members?

Answer: A new member would be required to comply with the minimum net capital requirements in effect at the time the firm becomes a member of the NASD, including the temporary phase-in minimums.

Question #23: May a firm that conducts a business in private debt and equity offerings, *where there is no clearing relationship*, but the firm promptly forwards all checks made out to the issuer, operate with a \$5,000 minimum net capital requirement?

Answer: Yes. The \$5,000 minimum net capital requirement is appropriate for this type of firm. However, if the offering involves any contingencies, the firm must comply with the provisions of SEC Rule 15c2-4. This firm may also

operate as an introducing broker.

Question #24: May a firm elect to accelerate the effectiveness of its minimum net capital requirement and report this final minimum requirement amount as its current requirement amount on the July 1, 1993, FOCUS Report?

Answer: No. A firm must follow the SEC’s temporary phase-in minimums for reporting its net capital requirement.

Question #25: If a firm falls in more than one category for determining minimum net capital requirements, which requirement would apply (e.g., a market maker that is also an introducing broker/dealer)?

Answer: A firm that engages in more than one type of business will be required to maintain a minimum net capital equal to the highest requirement for any business conducted. In the example given, the requirement would be the highest minimum associated with the firm’s market-making activities. Additionally, firms should be aware of the ratio requirements if computing net capital under the aggregate indebtedness method or the alternative method.

Question #26: What does “statutory underwriter” mean?

Answer: A statutory underwriter is any broker/dealer that is contractually committed to an issuer for the purchase of its securities.

Question #27: What is the minimum net capital requirement for an introducing firm participating in a firm-commitment underwriting, but not as an underwriter?

Answer: An introducing firm may participate in a firm-commitment

offering as a selling group member only, not committed to the issuer, and operate under the \$50,000 minimum net capital requirement.

Question #28: Did the haircuts for equity securities change on January 1, 1993?

Answer: Yes. All firms, whether they compute net capital under the basic method or the alternative method, now compute equity haircuts the same, that is, 15 percent of the market value of the greater of the long or short position and, if the lesser position exceeds 25 percent of the greater position, an additional 15 percent is taken on the excess amount. This treatment applies to all securities in paragraph

(c)(2)(vi)(J) "All Other Securities." For those equity securities that are included in paragraph (c)(2)(vi)(K)(ii) the haircut remains 40 percent.

Question #29: Did the method for determining undue concentration deductions change on January 1, 1993?

Answer: Yes. All firms, whether they compute net capital under the basic method or the alternative method must compute undue concentration deductions pursuant to paragraph (c)(2)(vi)(M). For equities and debt securities, the deduction must be applied immediately, except for securities underwritten (for which the deduction is not

applied until after 11 business days).

Question #30: Is there any relief given to the aggregate indebtedness charge of $6\frac{2}{3}$ percent for firms that conduct a mutual fund business?

Answer: Yes. If a broker/dealer has a payable to a mutual fund that is related to a fail-to-deliver receivable of the same quantity, 85 percent of that liability would be excluded from aggregate indebtedness. Additionally, similar aggregate indebtedness relief will be afforded stock loan payables that are offset by stock borrowed receivables of the same quantity and issue.

NASD NOTICE TO MEMBERS 93-31

SEC Requests Comments on Proposal To Establish Three- Business-Day Settlement For Securities Transactions

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

In the March 1, 1993, edition of the *Federal Register*, the Securities and Exchange Commission (SEC) published notice of its intention to adopt Rule 15c6-1 under the Securities Exchange Act of 1934. This new rule would establish three, instead of five, business days as the standard settlement time-frame for broker/dealer transactions. The proposed rule is intended to reduce the risks associated with unsettled securities transactions. It is contemplated that shortening the settlement cycle will decrease the total number of unsettled trades at any given time, thereby benefiting broker/dealers, clearing corporations, and public investors. The SEC is requesting comments on the proposed rule as well as whether its proposed effective date of January 1, 1996 provides sufficient time to implement the necessary changes efficiently. Comments on the proposed rule are due on or before June 30, 1993.

Background

In the United States, the settlement cycle varies among markets. Settlement in the futures, options, and government securities markets occurs on the day after trade date using same-day funds. On the other hand, settlement of most trades in corporate and municipal securities takes place on the fifth business day after the trade date (T+5), with payment in next-day funds. Settling securities transactions on T+5 is largely a function of market custom and industry practice. Although the rules of the NASD and other self-regulatory organizations define "regular way" settlement as T+5, no federal rule mandates a specific settlement cycle for securities transactions.

Following the market break of October 1987, the clearance and settlement system came under close scrutiny as several government and industry groups sought to identify causes for the market decline and develop initiatives to protect market participants from the impact of such declines in the future.

The Group of Thirty conducted one of these studies. The Group is an independent, non-partisan, non-profit organization composed of international financial leaders whose focus is on international economic and financial issues. In March 1989, the Group of Thirty issued a report with a number of proposals to improve clearance and settlement practices and standards. Among these proposals was the recommendation that settlement take place on the third day after trade date (T+3).

Following release of this report, the United States formed two subcommittees, the U.S. Steering Committee and a U.S. Working Committee of the Group of Thirty, to evaluate these recommendations. The subcommittees concluded that shortening the settlement cycle and converting to the use of same-day funds would be beneficial.

The SEC convened a round table to discuss the subcommittee's recommendations. Round table participants generally agreed that these recommendations should be adopted but expressed concern about the impact on broker/dealers conducting a predominantly retail business. Subsequently, at the request of SEC Chairman Richard Breeden, an industry task force, headed by John W. Bachmann, the Managing Principal of Edward D. Jones & Co. of St. Louis, Missouri, undertook an independent evaluation of these issues.

In May 1992, the Bachmann Task Force presented its findings to the SEC. These findings supported T+3 settlement. The SEC published the Bachmann Task Force Report in the *Federal Register* on June 22, 1992, and requested public comment on the recommendations.

The SEC received 1,000 comment letters from banks, broker/dealers, investment advisers, trade associations, clearing agencies, exchanges, transfer agents, and individual investors. Although generally supportive, many commentators questioned how these changes would be implemented, expressing particular concern about the potential elimination of physical certificates. Many of the issues noted by the commentators were also identified by the Bachmann Task Force. Although the SEC's efforts to address them are nearing completion, the Commission will consider comments on the Bachmann Task Force Report recommendations in connection with this proposal.

Description of Proposed Rule 15c6-1

Proposed Rule 15c6-1 provides that, unless otherwise expressly agreed to by the parties at the time of the transaction, a broker or dealer is prohibited from entering into a contract for the purchase or sale of a security (other than an exempted security, government security, municipal security, commercial paper, bankers' acceptances, or commercial bills) that provides for

payment of funds and delivery of securities later than the third business day after the date of the contract.

It should be noted that the proposed rule allows a broker or dealer to agree that settlement will occur in more or less than three business days, provided the agreement is explicit and reached at the time of the transaction. However, this is not intended to require broker/dealers to specify all contract terms before a trade is executed.

The proposed rule does not affect the ability of individual investors to obtain a physical certificate. The rule also does not specifically address settlement in same-day funds. However, various self-regulatory organizations currently are working on a number of initiatives to accomplish this goal.

The SEC is requesting comment on whether the scope of the proposed rule is appropriate and whether any particular characteristics of different types of securities (e.g., mutual fund shares and limited partnership interests) will create difficulties for broker/dealers and investors if included in or excluded from the rule. In particular, the SEC is seeking comment on the most appropriate way and a reasonable time frame for bringing municipal securities within the scope of the rule.

The SEC also is seeking comment on the proposed implementation date of January 1, 1996, which allows broker/dealers a three-year

period in which to make necessary changes. Interested persons are also asked to comment on whether January 1, 1995, or July 5, 1995, would be appropriate alternative implementation dates.

NASD members that wish to comment on the proposed rule should do so by June 30, 1993. Comment letters should refer to File No. S7-5-93 and should be sent, in triplicate, to:

Jonathan G. Katz
Secretary
Securities and Exchange
Commission
450 Fifth Street, NW
Mail Stop 6-1
Washington, DC 20549.

The Commission will make all comments available for public inspection and copying at its Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. 20549.

Members are requested to send copies of their comment letters to:

Stephen D. Hickman
Corporate Secretary
National Association of
Securities Dealers, Inc.
1735 K Street, NW
Washington, DC 20006-1500.

Questions concerning this Notice may be directed to Walter J. Robertson, Director, Compliance, at (202) 728-8236 or Samuel Luque, Associate Director, Compliance, at (202) 728-8472.

NASD NOTICE TO MEMBERS 93-32

NASD Publishes *Sanction Guidelines* To Familiarize Members With Major Violations And Penalties

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD announces the publication of the *NASD Sanction Guidelines (Guidelines)*. The *Guidelines* are being published so that members may become more familiar with some of the typical securities industry violations that occur and the disciplinary sanctions that may result.

Background

The *Guidelines* are being published and distributed so that members may become more familiar with some of the typical securities industry rule violations that occur and the disciplinary sanctions that may result. The *Guidelines* address more than 40 different types of violations.

Originally disseminated by the NASD National Business Conduct Committee (NBCC) for use by the various NASD District Business Conduct Committees and the Market Surveillance Committee, the *Guidelines* help the committees decide on appropriate remedial sanctions in NASD disciplinary proceedings. The *Guidelines* are not, however, predetermined, fixed sanctions for particular violations. Rather, they serve as a guide for the committees in an effort to achieve greater consistency, uniformity, and fairness when imposing sanctions.

Developed for the most frequent violations, the *Guidelines* include a listing of the basic considerations concerning the gravity of an offense and discuss a range of appropriate sanctions. Depending on the mitigating or aggravating factors present in individual cases, sanctions may be increased or decreased beyond the limits set forth in the *Guidelines*.

A significant consideration in determining appropriate sanctions for each type of violation listed in the *Guidelines* is a respondent's history of similar misconduct. This reflects the NBCC's belief that a primary objective of the NASD disciplinary process is to deter future violations by imposing progressively escalating sanctions upon repeat violators.

For more information on the *Guidelines*, call Norman Sue, Jr., Associate General Counsel, at (202) 728-8117, or Lewis E. Antone, Jr., Attorney, at (202) 728-8245. In addition to the enclosed copy of the *Guidelines*, additional copies of the *Guidelines* are available for purchase at \$35 each (\$10 each for employees of NASD member firms) by contacting NASD MediaSourceSM at (301) 590-6578 for credit card orders or by writing to: NASD, NASD MediaSource, P.O. Box 9403, Gaithersburg, MD 20898-9403. Please make checks payable to the National Association of Securities Dealers, Inc.

NASD NOTICE TO MEMBERS 93-33

The Role of the NASD's Disciplinary Committees

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The cornerstone of the NASD's self-regulatory process is the nationwide committee system of securities industry representatives that conducts peer reviews, takes disciplinary action where appropriate, and imposes remedial sanctions when federal securities laws or NASD® rules and regulation have been violated. When considering disciplinary matters, these key committees located in each of the NASD's 11 districts sit as District Business Conduct Committees (DBCC), the primary local enforcement arm of the NASD. The Market Surveillance Committee (MSC) performs a similar function, but acts as the central review body for cases involving possible violations of market-related NASD and SEC rules.

Background

Established by the 1938 Maloney Act Amendments to the Securities Exchange Act of 1934 (Act), the NASD is the nation's largest self-regulatory organization, and therefore is a key component of the federally supervised self-regulation of the securities industry.

As congressionally mandated, the NASD's chief duty is that of a regulator. The NASD fulfills its statutory responsibilities and protects the investing public through enforcement of federal securities laws as well as the broader ethical requirements of NASD rules, which are designed to prevent fraudulent and manipulative acts and practices, and to promote just and equitable principles of trade. The NASD exercises this statutory authority over members and their associated persons by administering qualification examinations, conducting compliance inspections, and taking appro-

priate disciplinary actions when necessary.

A principal means by which the NASD fulfills its regulatory responsibilities is through the NASD disciplinary process which seeks to determine whether a member firm or its associated persons have violated NASD rules and regulations, or the federal securities laws.

NASD disciplinary proceedings help to protect the public investor and promote member compliance by imposing a range of sanctions on those who fail to comply. Respondents are afforded an impartial hearing before their peers and have extensive rights of appeal. Members and persons associated with members involved in an NASD disciplinary action may be subject to sanctions that include fines, censure, suspensions, bars, expulsion, restitution, or any other fitting sanction.

The NASD provides a fair procedure for disciplining members and associated persons that is consistent with the due process standards established by the statute. NASD disciplinary proceedings are remedial actions conducted in a businessman's forum.

Though not subject to the same procedural standards as courts of law, the NASD ensures compliance with fundamental legal standards of fairness through an established process. For example, the statute specifies safeguards that at minimum require the NASD to: bring specific charges; give notice of such charges; provide an opportunity to defend; keep a record; and, specify in any adverse determination the act or practice that constituted a violation, the provision violated, the sanction imposed, and the accompanying reason for sanction.

NASD Disciplinary Bodies

The Board of Governors

The Board of Governors is the controlling body of the NASD and determines policy on a national scale. The Board consists of Governors elected by member firms from the 11 districts throughout the United States, and Governors-at-Large elected by the Board to represent investors, Nasdaq®-listed companies, insurance company members, investment company underwriters, and the securities industry at large.

The National Business Conduct Committee (NBCC)

Consisting of first-year members of the Board of Governors, the NBCC's chief function is to ensure that disciplinary actions taken by the NASD's DBCCs and MSC are legally sufficient and consistent with NASD and federal policy.

The NBCC helps set regulatory policy, reviews all DBCC and MSC decisions, and hears cases appealed to the Board of Governors by respondents named in these actions. On its own motion, the NBCC may call any DBCC or MSC decision for review. All decisions of the NBCC are final unless called for review by a member of the Board of Governors.

District Committees And DBCCs

There are 11 geographical districts, each of which is governed by a District Committee composed of individuals elected locally in each region by NASD members. When considering disciplinary matters, a District Committee sits as a DBCC, the primary local enforcement arm of the NASD. These committees meet in each district, and enforce

compliance by members in their geographical area with:

- NASD By-Laws and Rules of Fair Practice.
- Federal securities law.
- The Municipal Securities Rulemaking Board (MSRB) rules.
- Other applicable securities regulations.

Market Surveillance Committee (MSC)

The MSC is a national committee that acts as the central review body for investigations conducted by the Market Surveillance and Anti-Fraud Departments that involve possible violations of market-related NASD and SEC rules, including insider trading, market manipulation, and other egregious or fraudulent market conduct. As a disciplinary committee, the MSC's authority is identical to that of the DBCC.

NASD Disciplinary Process

Empowered by the Board of Governors, each DBCC and MSC review is the first step in the NASD's disciplinary process.

District examiners in the field report to the DBCC regarding member compliance with the aforementioned rules and regulations based on information collected through various examination and surveillance programs.

In fulfilling their enforcement responsibilities, the 11 DBCCs and the MSC:

- Review examination reports and other investigative summaries submitted by NASD staff in their respective districts or departments.

- Initiate or authorize complaints against firms or associated persons alleged to have violated NASD rules or other rules over which the NASD has jurisdiction.

- Conduct disciplinary proceedings in accordance with the NASD's Code of Procedure.

- Render decisions and impose sanctions, if appropriate.

Serving on a DBCC or MSC

Annually, the NASD conducts elections to replace those DBCC and MSC members whose three-year terms expire at year-end. NASD members are eligible to vote for those candidates seeking election to their respective district committees. If you are interested in serving on the DBCC in your district or have any questions about the DBCC process, please contact the appropriate District Director listed below.

NASD District Offices

District 1

525 Market Street, Suite 300
San Francisco, CA 94105-2711
(415) 882-1200
FAX: (415) 546-6991
Elisabeth P. Owens, Dir.

Northern California (the counties of Monterey, San Benito, Fresno, and Inyo, and the remainder of the state north or west of such counties), northern Nevada (the counties of Esmeralda and Nye, and the remainder of the state north or west of such counties), and Hawaii

District 2

300 South Grand Avenue
Suite 1600
Los Angeles, CA 90071
(213) 627-2122
FAX: (213) 617-3299
Daniel Stefek, Asst. Dir.
Lani Wolmann, Regional Counsel

Southern California (that part of the state south or east of the counties of Monterey, San Benito, Fresno, and Inyo) and southern Nevada (that part of the state south or east of the counties of Esmeralda and Nye)

District 3 (Denver)

1401 17th Street, Suite 700
Denver, CO 80202
(303) 298-7234
FAX: (303) 292-4272
Frank Birgfeld, Dir.

Arizona, Colorado, New Mexico, Utah, and Wyoming

District 3 (Seattle)

Two Union Square
601 Union Street, Suite 1616
Seattle, WA 98101
(206) 624-0790
FAX: (206) 624-0790
James G. Dawson, Assoc. Dir.

Alaska, Idaho, Montana, Oregon, and Washington

District 4

12 Wyandotte Plaza
120 West 12th Street
Suite 900
Kansas City, MO 64105
(816) 421-5700
FAX: (816) 421-5029
Jack Rosenfield, V.P. Dir.

Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, and South Dakota

District 5

1100 Poydras Street
Suite 850, Energy Centre
New Orleans, LA 70163
(504) 522-6527
FAX: (504) 581-3699
Warren A. Butler, Jr., Dir.

Alabama, Arkansas, Kentucky, Louisiana, Mississippi, Oklahoma, and Tennessee

District 6

1999 Bryan Street, Suite 1450
Olympia & York Tower
Dallas, TX 75201
(214) 969-7050
FAX: (214) 922-0079
Peter M. Walker, Dir.

Texas

District 7

One Securities Centre
Suite 500
3490 Piedmont Road, NE
Atlanta, GA 30305
(404) 239-6100
FAX: (404) 237-9290
Marilyn B. Davis, Dir.

Florida, Georgia, North Carolina, South Carolina, Puerto Rico, the Canal Zone, and the Virgin Islands

District 8 (Chicago)

10 S. LaSalle St., 20th Floor
Chicago, IL 60603-1002
(312) 899-4400
FAX: (312) 236-3025
E. Craig Dearborn, V.P., Dir.

Illinois, Indiana, Michigan, and Wisconsin

District 8 (Cleveland)

Renaissance on Playhouse Sq.
1350 Euclid Ave., Suite 900
Cleveland, OH 44115
(216) 694-4545
FAX: (216) 694-3048
William H. Jackson, Jr., Dir.

Ohio and part of upstate New York (the counties of Monroe, Livingston, and Steuben; and the remainder of the state west of such counties)

District 9 (Philadelphia)

1818 Market Street, 14th Floor
Philadelphia, PA 19103
(215) 665-1180
FAX: (215) 496-0434
John P. Nocella, V.P., Dir.

Delaware, Pennsylvania, West Virginia, and southern New Jersey (the counties of Atlantic, Burlington, Camden, Cape May, Cumberland, Gloucester, Mercer, Ocean, and Salem)

District 9 (Washington, DC)

1735 K Street, NW
Washington, DC 20006-1500
(202) 728-8400
FAX: (202) 728-8890
Brian Hobbs, Assoc. Dir.

District of Columbia, Maryland, and Virginia

District 10

33 Whitehall Street
New York, NY 10004
(212) 858-4000
FAX: (212) 858-4189
Douglas Henderson, Sr. V.P., Dir.

The five boroughs of New York City and the adjacent counties in New York (the counties of Nassau, Orange, Putnam, Rockland, Suffolk, Westchester) and northern New Jersey (the state of New Jersey, except for the counties of Atlantic, Burlington, Camden, Cape May, Cumberland, Gloucester, Mercer, Ocean, and Salem)

District 11

260 Franklin St., 16th Floor
Boston, MA 02110
(617) 261-0800
FAX: (617) 951-2337
Willis Riccio, V.P., Dir.

Connecticut, Maine, Massachusetts,
New Hampshire, Rhode Island,
Vermont, and New York (except for
the counties of Nassau, Orange,
Putnam, Rockland, Suffolk, and
Westchester; the counties of
Monroe, Livingston, and Steuben;
the remainder of the state west of
such counties; and the five
boroughs of New York City)

If you are interested in serving on
the Market Surveillance Committee
please contact:

James J. Cangiano
Senior Vice President
Market Surveillance Department
9513 Key West Ave.
Rockville, MD 20850-3389
(301) 590-6424.

NASD NOTICE TO MEMBERS 93-34

As of April 23, 1993, the following 53 issues joined the Nasdaq National Market,[®] bringing the total number of issues to 3,065:

Nasdaq National Market[®]
Additions, Changes,
And Deletions as of
April 23, 1993

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Symbol	Company	Entry Date	SOES Execution Level
JARS	Alltrista Corporation	3/24/93	1000
CHCS	Chico's FAS, Inc.	3/24/93	1000
FFBG	First Federal Savings Bank of Brunswick Georgia	3/24/93	200
SUMIZ	Sumitomo Bank of California (The) (Dep Shrs)	3/24/93	1000
APSG	Applied Signal Technology, Inc.	3/26/93	1000
BKST	Brookstone, Inc.	3/26/93	200
GILTF	Gilat Satellite Networks Ltd.	3/26/93	1000
UBSC	Union Bankshares, Ltd.	3/26/93	1000
WDSTW	WordStar Int'l Corporation (3/26/96 Wts)	3/26/93	500
FSCX	Fastcomm Communications Corporation	3/29/93	1000
NSAI	NSA International, Inc.	3/29/93	500
LSSI	Leasing Solutions, Inc.	3/30/93	500
PLLN	Parallan Computer, Inc.	3/30/93	1000
PCAM	Physician Corporation of America	3/30/93	1000
BROC	Brock Control Systems, Inc.	3/31/93	500
GYMB	Gymboree Corporation (The)	3/31/93	1000
LIBT	Liberty Technologies, Inc.	3/31/93	200
OSHC	Orchard Supply Hardware Stores Corporation	3/31/93	1000
BANF	BancFirst Corporation	4/1/93	1000
CGFC	Coral Gables Fedcorp, Inc.	4/1/93	1000
DAVD	Davidson & Associates, Inc.	4/1/93	500
ENVI	Envirotest Systems, Inc. (CI A)	4/1/93	1000
ETHCY	Ethical Holdings plc (ADR)	4/1/93	1000
XLTCZ	Excel Technology, Inc. (9/30/97 CI A Wts)	4/1/93	500
MSDX	Mason-Dixon Bancshares, Inc.	4/1/93	200
SUBI	Sun Bancorp, Inc.	4/1/93	200
HFSB	Hamilton Bancorp, Inc.	4/2/93	1000
INHM	Inco Homes Corporation	4/2/93	1000
WCTI	WCT Communications, Inc.	4/2/93	1000
CSDS	Casino Data Systems	4/5/93	1000
CBVA	Commerce Bank	4/5/93	1000
KCLC	Kinder-Care Learning Centers, Inc.	4/5/93	1000
KCLCW	Kinder-Care Learning Centers, Inc. (4/1/97 Wts)	4/5/93	500
SUNY	Sunrise Bancorp, Inc.	4/5/93	1000
SHEN	First Shenango Bancorp, Inc.	4/6/93	500
BHCF	BHC Financial, Inc.	4/7/93	1000
FOSL	Fossil, Inc.	4/8/93	1000
JSBA	Jefferson Savings Bancorp, Inc.	4/8/93	1000

Symbol	Company	Entry Date	SOES Execution Level
NFOR	NFO Research, Inc.	4/8/93	1000
EDNTF	Edunetics Ltd.	4/13/93	500
PAUH	Paul Harris Stores, Inc.	4/14/93	1000
SAFT	Safety 1st, Inc.	4/14/93	1000
SANM	Sanmina Corp.	4/14/93	1000
NCSIW	National Convenience Stores Inc. (3/9/98 Wts)	4/15/93	1000
WIND	Wind River Systems, Inc.	4/15/93	1000
EQNX	Equinox Systems Inc.	4/16/93	1000
TCBK	TriCo Bancshares	4/19/93	500
MRCF	Martin Color-Fi, Inc.	4/21/93	1000
SWSH	Swisher International, Inc.	4/21/93	500
SWSHW	Swisher International, Inc. (4/21/96 Wts)	4/21/93	500
DBII	Digital Biometrics, Inc.	4/22/93	1000
WBAN	West Coast Bancorp, Inc.	4/22/93	200
ORLY	O'Reilly Automotive, Inc.	4/23/93	500

Nasdaq National Market Symbol and/or Name Changes

The following changes to the list of Nasdaq National Market securities occurred since March 22, 1993:

New/Old Symbol	New/Old Security	Date of Change
DOSEW/DOSEW	Choice Drug Systems Inc. (9/30/93 Wts)/Choice Drug Systems Inc. (3/31/93 Wts)	3/24/93
JSBK/JSBK	Johnstown Savings Bank/Johnstown Savings Bank FSB	3/24/93
BNKS/BNKS	First United Bank Group, Inc./United New Mexico Financial Corp.	3/26/93
PACE/AMGP	Pace American Group/American Insurance Group, Inc.	3/31/93
COBR/DYNA	Cobra Electronics Corp./Dynascan Corp.	4/1/93
XLTCZ/XLTCW	Excel Technology, Inc. (9/30/97 Wts Cl A)/Excel Technology, Inc. (9/30/97 Wts Cl A)	4/2/93
JARS/JARSV	Alltrista Corp./Alltrista Corp. (WI)	4/6/93
NCELW/NCELW	Nationwide Cellular Service, Inc. (5/17/93 Wts)/Nationwide Cellular Service, Inc. (4/12/93 Wts)	4/6/93
JMCG/SFNS	Spear Financial Services, Inc./Spear Financial Services, Inc.	4/6/93
NCSI/NCSIV	National Convenience Stores Inc. (4/21/93 WI)/National Convenience Stores Inc. (WI)	4/15/93
CMPC/BYTE	CompuCom Systems, Inc./CompuCom Systems, Inc.	4/19/93
ARTL/FCON	Aristotle Corp. (The)/First Constitution Financial Corp.	4/19/93
BHAG/BHAGA	BHA Group, Inc. (Cl A)/BHA Group, Inc. (Cl A)	4/22/93
KCLCW/KCLW	Kinder-Care Learning Centers (4/1/97 Wts)/Kinder-Care Learning Centers 4/1/97 (Wts WI)	4/22/93
KCLC/KCLCV	Kinder-Care Learning Centers, Inc./Kinder-Care Learning Centers, Inc. (WI)	4/22/93
SDYNW/SDYNW	Stadyn Inc. (6/19/94 Wts)/Stadyn Inc. (6/19/93 Wts)	4/22/93

Nasdaq National Market Deletions

Symbol	Security	Date
FFPR	First Federal Savings Bank P.R.	3/24/93
HESI	Hunter Environmental Services, Inc.	3/24/93
MTRC	Mercantile Bancorp Inc.	3/26/93
CLACB	Colonial Companies, Inc. (CI B)	3/29/93
IFEI	Imagine Films Entertainment, Inc.	3/30/93
UBANP	US Bancorp Inc. (Pfd)	3/30/93
NESB	NESB Corporation	3/31/93
VNCP	Valley National Corporation	3/31/93
RODS	American Steel and Wire Corporation	4/1/93
MSBI	Montclair Bancorp Inc.	4/2/93
FSEIC	FIRST SEISMIC Corporation	4/5/93
MAINW	Main St. & Main Inc. (9/4/96 Wts)	4/12/93
HRIZ	Horizon Resources Corporation	4/15/93
ATTC	Auto-Trol Technology	4/16/93
KENCA	Kentucky Central Life Insurance Co. (CI A)	4/16/93
MSCO	Masstor Systems Corporation	4/19/93
DUSAW	Deprenyl USA, Inc. (4/19/93 CI A Wts)	4/20/93
BHAGB	BHA Group, Inc. (CI B)	4/22/93
RSLA	Republic Capital Group, Inc.	4/22/93
TSLQE	TSL Holdings, Inc.	4/23/93

Questions regarding this Notice should be directed to Mark A. Esposito, Supervisor, Market Listing Qualifications, at (202) 728-8002. Questions pertaining to trade-reporting rules should be directed to Bernard Thompson, Assistant Director, NASD Market Surveillance, at (301) 590-6436.

NASD DISCIPLINARY ACTIONS

Disciplinary Actions Reported for May

The NASD® is taking disciplinary actions against the following firms and individuals for violations of the NASD Rules of Fair Practice; securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board. Unless otherwise indicated, suspensions will begin with the opening of business on Monday, May 17, 1993. The information relating to matters contained in this Notice is current as of the fifth of this month. Information received subsequent to the fifth is not reflected in this publication.

Firms Expelled, Individuals Sanctioned

First Choice Securities Corp. (Englewood, Colorado), Gregory F. Walsh (Registered Principal, Los Angeles, California), Derek H. Yamada (Registered Principal, Denver, Colorado), and Sheldon O. Fertman (Registered Principal, Denver, Colorado). The firm was fined \$200,000 and expelled from membership in the NASD. Walsh was fined \$25,000, suspended from association with any NASD member in any capacity for two years, and required to requalify by examination in any capacity that he desires to act after his suspension. Yamada was fined \$50,000 and barred from association with any NASD member in any capacity.

The sanctions were based on findings that the firm conducted a securities business while failing to maintain its minimum required net capital and filed an inaccurate FOCUS Part I report. The firm also violated Securities and Exchange Commission (SEC) Rule 15c2-6, by effecting transactions in designated securities in the accounts of public customers without obtaining suitability statements and other infor-

mation required by the rule before approving their accounts. Furthermore, the firm failed to respond to NASD requests for information, allowed an unregistered person to act as a principal of the firm, and failed to disclose on the firm's Form BD that this individual was a control person with the firm.

In addition, the firm, acting through Walsh and Yamada, failed to make a bona fide "minimum-maximum" contingent offering of limited partnership interests in that they effected the sale of 18 percent of the total amount of the securities being offered to accounts that were related to the issuer for non-investment purposes to meet the minimum number of units required to close the offering, and failed to disclose the purpose of these sales to investors. The firm, acting through Yamada, purchased securities while participating as an underwriter in the same stock's distribution during its initial public offering (IPO). They also induced customers to purchase these securities at excessive prices while failing to disclose to the customers that they were purchasing the securities at excessive prices compared to the prices in the IPO.

The firm, acting through Yamada, falsified order tickets relating to securities transactions in the same stock by causing notations of dealers whom they contacted as market makers in the securities, and quotations that they received from the dealers relating to the securities, to be reflected on the order tickets when, in fact, these dealers were not market makers in the security and were not providing quotations in the security.

In addition, the firm, acting through Walsh, failed to establish, maintain, and enforce written supervisory

procedures to prevent the aforementioned violations, and filed an inaccurate Form BD that represented to the NASD that the firm was wholly owned by a company that did not exist.

In a separate action, First Choice and Fertman were fined \$114,088, jointly and severally and the firm was suspended from all principal transactions for 60 days. Fertman was barred from association with any NASD member in any capacity.

The sanctions were based on findings that the firm, acting through Fertman, effected principal sales of securities to public customers at unfair and unreasonable prices based on all relevant circumstances. These circumstances included the fact that the firm was not a market maker in the securities at the time the trades were effected and that the markups on these trades ranged from 76 to 100 percent over the firm's contemporaneous cost for the securities. Moreover, the firm, acting through Fertman, failed to disclose the unfair and unreasonable prices to the customers.

Smith Bellingham International, Inc. (San Francisco, California) and **Michael William Meagher (Registered Principal, Mill Valley, California)** were fined \$9,200, jointly and severally, and fined \$15,000, jointly and severally with another registered representative. The firm was fined an additional \$35,000, expelled from NASD membership, and fined \$20,000, jointly and severally with a registered representative. Furthermore, Meagher was fined \$35,000 and barred from association with any NASD member in any capacity.

The sanctions were based on findings that the firm, acting through Meagher, failed to comply with the SEC Customer Protection Rule

15c3-3 by receiving and accepting customer funds in violation of its claimed exemption from the rule and did not otherwise comply with the full provisions of the rule. In addition, the firm, acting through Meagher, offered and sold units of convertible notes by means of false and misleading statements of material fact and omissions of material fact. Specifically, the respondents represented to investors that the proceeds of an offering would be used to purchase capital equipment, to develop a management team, to provide working capital for new product development, and to allow the company to build up its inventory. However, the respondents failed to disclose to prospective purchasers that the proceeds were used to retire pre-existing debt.

Furthermore, the firm, acting through Meagher, permitted an individual to act as a representative of the firm without proper registration and failed to evidence supervisory review and approval of securities transactions effected by the firm. Moreover, the firm failed to file its quarterly FOCUS Part IIA reports in a timely manner.

Firms Fined, Individuals Sanctioned

Aimco Securities Company, Inc. (San Diego, California), Marvin Irwin Friedman (Registered Principal, La Jolla, California), and William Raymond Braun (Registered Principal, La Mesa, California) submitted an Offer of Settlement pursuant to which the firm was fined \$20,000. Friedman was fined \$20,000 and barred from association with any NASD member in any proprietary or principal capacity, and Braun was fined \$10,000 and suspended from association with any NASD member as a financial and operations principal

for one year.

Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Friedman and Braun, conducted a securities business while failing to maintain its minimum required net capital and continued to conduct business when they knew, or should have known, that the firm did not have sufficient net capital.

First Gateway Securities, Inc. (St. Louis, Missouri) and Kenneth Keith Kays (Registered Principal, Fenton, Missouri) were fined \$20,000, jointly and severally. In addition, the firm and Kays were each fined \$2,222 and required to undergo staff interviews. First Gateway was also fined \$2,500, jointly and severally with another respondent and Kays was required to requalify by examination as a principal. The National Business Conduct Committee (NBCC) imposed the sanctions following an appeal of a District 4 District Business Conduct Committee (DBCC) decision. The sanctions were based on findings that the firm, acting through Kays, effected transactions with public customers at unfair prices with markups ranging from 6.42 to 20 percent above the firm's contemporaneous costs. They also charged excessive and unfair commissions ranging from 5.25 to 20.64 percent in agency transactions.

The firm, acting through Kays, failed to comply with its restriction agreement with the NASD in that it opened and operated a branch office without notifying or obtaining approval from the NASD. In addition, the firm, acting through Kays, executed principal transactions and violated its restriction agreement by maintaining a trading inventory in

shares of a common stock. Furthermore, the firm inaccurately prepared its books and records.

Lowell H. Listrom & Company, Inc. (Kansas City, Missouri), Lowell H. Listrom (Registered Principal, Kansas City, Missouri) and Stephen L. Mock (Registered Principal, Grandview, Missouri) were fined \$15,000, jointly and severally. In addition, Listrom was suspended from association with any NASD member in any capacity for two weeks. The SEC affirmed the sanctions following an appeal of a March 1988 NBCC decision.

The sanctions were based on findings that the firm, acting through Listrom and Mock, made improper withdrawals from the Special Reserve Bank Account for the Exclusive Benefit of Customers when the required computations made before the withdrawals either did not permit any withdrawal or permitted a withdrawal that was significantly less than the amount actually withdrawn. Furthermore, the respondents made deposits to the reserve account from an overdrawn bank account.

In addition, the firm, acting through Listrom, failed to maintain the required minimum margin in two customer accounts.

Firms and Individuals Fined

GBM International, Inc. (Houston, Texas) and Julio Carlos Marron (Registered Principal, Houston, Texas) submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were fined \$51,187.75, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanction and to the entry of findings that, in violation of the Interpretation of the

Board of Governors concerning Free-Riding and Withholding, the firm, acting through Marron, purchased and sold shares of a "hot issue."

Sunpoint Securities, Inc. (Longview, Texas) and Van Roberson Lewis, III (Registered Principal, Longview, Texas) submitted an Offer of Settlement pursuant to which they were fined \$15,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanction and to the entry of findings that the firm, acting through Lewis, failed to comply with Schedule C of the NASD's By-Laws in that they allowed two individuals at the firm to effect securities transactions with public customers and to receive commissions for the transactions when their registrations with the NASD had not been approved.

The findings also stated that the firm, acting through Lewis, effected purchases of designated securities for public customers without obtaining from each customer a written suitability statement and a written agreement to the transaction, in violation of SEC Rule 15c2-6. In addition, the NASD found that the firm, acting through Lewis, failed to establish adequate written supervisory procedures or to properly supervise the firm's compliance with SEC Rule 15c2-6.

Yankee Financial Group, Inc. (Bright Waters, New York) and Richard F. Kresge (Registered Principal, Bayshore, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were fined \$10,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanction and to the entry of findings that the firm, act-

ing through Kresge, executed 29 municipal securities transactions on a riskless principal basis and 22 option transactions with public customers without an effectively registered municipal securities principal or options principal.

Individuals Barred or Suspended

Angie Theresa Agarpao (Associated Person, Mountain View, California) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Agarpao submitted to a member firm an examination score report that falsely reflected a passing score when, in fact, she had failed the Series 6 examination. Agarpao also failed to respond to NASD requests for information.

Douglas Drake Alcalá (Registered Representative, Seattle, Washington) submitted Offers of Settlement pursuant to which he was fined \$2,500, suspended from association with any NASD member in any capacity for 60 days, and must disgorge \$7,500 to the NASD. In a separate Offer of Settlement, Alcalá was suspended from association with any NASD member in any capacity for an additional period of 90 days and must disgorge \$1,500 to the NASD.

Without admitting or denying the allegations in both proceedings, Alcalá consented to the described sanctions and to the entry of findings that he recommended and executed transactions in the accounts of public customers without having reasonable grounds for believing that such recommendations were suitable for the customers.

Bruce B. Angus (Registered Representative, Hohenwald,

Tennessee) was fined \$70,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Angus misappropriated to his own use and benefit insurance customer funds totaling \$14,472.08. In addition, Angus failed to respond to NASD requests for information.

Michael J. Becal (Registered Representative, Margate, Florida) was fined \$25,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Becal failed to respond to NASD requests for information.

William Munroe Boland, Jr. (Registered Principal, New York, New York) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Boland failed to respond to NASD requests for information.

Pal Boquist (Registered Principal, Treasure Island, Florida) was fined \$25,000, barred from association with any NASD member in any capacity, and required to pay \$6,000 in restitution to a public customer. The sanctions were based on findings that Boquist engaged in a private securities transaction without providing prior written notice to and receiving written authorization from his member firm. In addition, Boquist failed to respond to an NASD request for information.

Rocco A. Calise (Registered Representative, Johnston, Rhode Island) was fined \$40,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Calise misappropriated to his own use and benefit customer funds totaling \$4,290 without the knowledge or consent of his mem-

ber firm or the customers. In addition, Calise failed to respond to NASD requests for information.

Richard Emanuel Campbell (Registered Representative, Oakland, California) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$15,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Campbell consented to the described sanctions and to the entry of findings that he took a \$78.48 check without the knowledge or consent of the maker of the check (his supervisor).

Andrew William Casebeer (Registered Representative, Portland, Oregon) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$40,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Casebeer consented to the described sanctions and to the entry of findings that, without the clients' prior authorization or consent, he completed insurance policy surrender forms for 20 insurance customers requesting that their policies be surrendered and signed their names to those forms. The NASD determined that the surrender checks endorsed by Casebeer totaled \$34,803.22.

The NASD also determined that Casebeer received surrender checks for two other insurance customers who had completed policy surrender forms and endorsed the checks, totaling \$3,159.33, without the customers' prior knowledge or consent.

Thomas E. Cavanagh (Registered Representative, New York, New York) was fined \$20,000 and

barred from association with any NASD member in any capacity. The sanctions were based on findings that Cavanagh failed to provide testimony or to respond to NASD requests for information concerning transactions and activities he was involved in while employed at a member firm.

Thomas George Cecchi (Registered Representative, Grand Rapids, Michigan) was fined \$250,000, barred from association with any NASD member in any capacity, and required to pay \$129,611.89 in restitution to an insurance company. The sanctions were based on findings that Cecchi obtained funds totaling \$129,611.89 from 28 insurance customers by taking out loans from the customers' existing insurance policies. Cecchi informed the customers that he would use the loan proceeds in their entirety to finance the purchase of new life insurance policies. Contrary to what he told the customers, and without their knowledge or consent, Cecchi deposited the loan proceeds into an account that he controlled or had a beneficial interest in and retained the funds for his own use and benefit. Cecchi also failed to respond to NASD requests for information.

Robert Naylor Cherrington, Jr. (Registered Representative, San Francisco, California) was fined \$51,126 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Cherrington effected transactions in the accounts of public customers without their knowledge or consent and failed to respond to NASD requests for information.

Michael Joseph Clark (Registered Representative, Orchard Park, New York) submitted an Offer of Settlement pursuant

to which he was fined \$1,500 and suspended from association with any NASD member in any capacity for one business day. Without admitting or denying the allegations, Clark consented to the described sanctions and to the entry of findings that he failed to pay a \$7,000 NASD arbitration award.

Adam Jason Cohen (Registered Representative, New York, New York) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Cohen opened two fictitious accounts at his member firm and caused shares of a common stock to be purchased in the accounts to receive an advance on the commissions for the trades.

Peter Joseph Conley (Registered Representative, Anaheim Hills, California) was suspended from association with any NASD member in any capacity for seven days. The sanction was based on findings that, on several occasions, Conley placed orders to purchase securities with his member firm and failed to prepare order tickets for such transactions as required by the firm's written procedures. Moreover, after one of the orders was executed, the shares were placed in the firm's error account because no written order ticket had been submitted by Conley and the firm was unable to determine into whose customer account the securities should have been placed. Subsequent sale of the shares resulted in a \$10,000 loss to the firm.

Betty Lou Deislinger (Registered Representative, Little Rock, Arkansas) submitted an Offer of Settlement pursuant to which she was suspended from association with any NASD member in any capacity for one year. Without admitting or denying the allega-

tions, Deislinger consented to the described sanction and to the entry of findings that she recommended to public customers the purchase of various limited partnerships that were unsuitable and contrary to the customers' stated investment objectives of liquidity and safety of principal.

Kathleen C. Diedrich (Registered Representative, Waverly, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which she was fined \$10,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Diedrich consented to the described sanctions and to the entry of findings that she misappropriated insurance customer funds totaling \$2,696.34 intended as insurance premium payments without the knowledge or consent of the customers.

Francis A. Fisher, Jr. (Registered Representative, Cherry Hill, New Jersey) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Fisher failed to respond to NASD requests for information regarding customer complaints.

Patrick T. Flanagan (Registered Representative, Enfield, Connecticut) was fined \$10,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Flanagan failed to respond to NASD requests for information regarding customer complaints.

Steven L. Fritz (Registered Representative, Tulsa, Oklahoma) submitted an Offer of Settlement pursuant to which he was fined \$10,000, suspended from association with any NASD member in any capacity for four

months, and required to requalify by examination as a general securities representative.

Without admitting or denying the allegations, Fritz consented to the described sanctions and to the entry of findings that he provided a public customer with false and misleading written price quotes for an investment held in the customer's account. The NASD found that in an attempt to conceal these actions, Fritz provided the same customer with written valuations of his portfolio that were signed by a fictitious person. In addition, the NASD determined that Fritz gave the same customer a letter on which he forged the signature of an executive vice president of his member firm to further substantiate the false and misleading valuations.

Michael Demetrio Gabriele (Registered Representative, Chula Vista, California) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$260,000 and barred from association with any NASD member in any capacity. The fine may be reduced if Gabriele provides satisfactory evidence that he has paid \$210,000 to the appropriate parties.

Without admitting or denying the allegations, Gabriele consented to the described sanctions and to the entry of findings that he misused \$211,070 received from five public customers for investment purposes. According to the findings, Gabriele solicited these funds from investors by representing that he would provide them with an 11 percent return and gave each customer a document entitled "contract for a five-year money management account." The NASD determined that after a short while, Gabriele ceased making interest payments and, instead, used the funds collected to pay personal

expenses.

The findings also stated that Gabriele liquidated an investment for a customer, took the check, forged the recipient's signature, and deposited the check to his bank account.

Steven Douglas Grau (Registered Representative, Omaha, Nebraska) submitted an Offer of Settlement pursuant to which he was suspended from association with any NASD member in any capacity for five business days. The suspension will continue thereafter until an arbitration award has been paid or he has been discharged from payment. Without admitting or denying the allegations, Grau consented to the described sanction and to the entry of findings that he failed to pay a \$5,000 arbitration award plus \$1,092 in interest.

Patrick Lee Hamilton (Registered Representative, Burlingame, California) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Hamilton consented to the described sanctions and to the entry of findings that he effected an unauthorized transaction in a customer's account and failed to respond to NASD requests for information.

Alex L. Herman (Registered Principal, Denver, Colorado) was fined \$10,000 and suspended from association with any NASD member in any capacity for 90 days. The suspension will continue thereafter until Herman demonstrates that an arbitration award has been paid or, alternatively, that a payment schedule or other form of settlement has been agreed on. The sanctions were based on findings that Herman

failed to keep his Uniform Application for Securities Industry Registration or Transfer (Form U-4) current by failing to report his involvement in an arbitration proceeding. In addition, Herman failed to pay a \$47,013.87 NASD arbitration award.

Richard Albert Hernandez (Registered Representative, Torrance, California) was fined \$10,000 and suspended from association with any NASD member in any capacity for 90 days. The suspension will continue thereafter until an arbitration award has been satisfied. The sanctions were based on findings that Hernandez failed to pay in full a \$12,000 NASD arbitration award.

William Franklin Herndon (Registered Representative, Wichita, Kansas) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$7,500, suspended from association with any NASD member in any capacity for one month, and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Herndon consented to the described sanctions and to the entry of findings that, without prior knowledge or approval of his supervisors, he transmitted to various parties sales literature that was false and misleading, in that it was issued on the letterhead of the firm.

John Hoppe (Registered Representative, Albuquerque, New Mexico) was fined \$20,000 and barred from association with any NASD member in any capacity. In addition, Hoppe must pay \$3,575 in restitution to customers. The sanctions were based on findings that Hoppe obtained four checks totaling \$3,575 that were made payable to public customers,

forged the customers' signatures on the checks, and used these funds for his own benefit.

Deborah Lynn Jennings (Registered Representative, Fruitland, Idaho) was fined \$15,000, barred from association with any NASD member in any capacity, and required to pay \$1,620.74 in restitution to her member firm. The sanctions were based on findings that Jennings completed disbursement request forms for public customers requesting the surrender of their insurance policies. Acting without the customers' knowledge or consent, Jennings signed the customers' names on the forms, submitted the forms to her member firm, and received surrender checks totaling \$1,620.74.

Alan Kalupa (Registered Representative, Nutley, New Jersey) was fined \$50,000, barred from association with any NASD member in any capacity, and required to pay \$3,001.54 in restitution to his member firm. The sanctions were based on findings that Kalupa forged the signatures' of four insurance customers on disbursement request forms which he presented to his member firm. As a result, checks were issued from the customers' insurance policies totaling \$3,901.54. He converted these to his own use and benefit. In addition, Kalupa failed to respond to NASD requests for information.

Jeffrey L. Karlitz (Registered Representative, New York, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 10 days. Without admitting or denying the allegations, Karlitz consented to the described sanctions and to the entry of findings that he solicited a public

customer to purchase a common stock. However, after the purchase, the stock price dropped sharply. The NASD found that, Karlitz falsely represented to the customer the stock had not been purchased, and thereafter corrected the deficit in her account by transferring funds from the account of another public customer without the customer's consent.

Patrick G. Keel (Registered Representative, Bay St. Louis, Mississippi) was fined \$25,000 and barred from association with any NASD member in any capacity. The SEC affirmed the sanctions following an appeal of a December 1990 NBCC decision. The sanctions were based on findings that Keel recommended and executed unauthorized and unsuitable transactions in the accounts of public customers.

In addition, Keel exercised discretion in the accounts of public customers without obtaining their prior written authorization and without acceptance of the accounts as discretionary by his member firm. Furthermore, Keel recorded false information on a purchaser questionnaire and investor application to effect the purchase of a limited partnership by a public customer.

Raymond J. Kelleher (Registered Representative, Tarrytown, New York) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$50,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Kelleher consented to the described sanctions and to the entry of findings that he requested checks totaling \$13,782.72 against the policies of public customers, deposited the checks into his personal bank account, and used the funds for his own purposes without

the customers' knowledge or authorization.

Larry L. Lanier (Registered Representative, Atlanta, Georgia) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000 and suspended from association with any NASD member in any capacity for five business days. Without admitting or denying the allegations, Lanier consented to the described sanctions and to the entry of findings that he engaged in a private securities transaction with a public customer outside the scope of his association with his member firm and without providing written notification to and receiving written approval from his member firm.

Michael A. Largue (Registered Representative, Rockville Centre, New York) submitted an Offer of Settlement pursuant to which he was fined \$10,000, suspended from association with any NASD member in any capacity for two years, and must pay \$48,337.39 in restitution to his member firm. Without admitting or denying the allegations, Largue consented to the described sanctions and to the entry of findings that he falsified his previous commission records to secure employment with another member firm and obtain a 20 percent transitional signing bonus of \$48,337.39.

Alan Frederick Lipman (Registered Representative, Tucson, Arizona) submitted an Offer of Settlement pursuant to which he was suspended from association with any NASD member in any capacity for 30 days, barred from association with any NASD member in any principal capacity, and must requalify by examination. Without admitting or denying the allegations, Lipman consented to the described sanctions and to the entry of findings that he falsified his

member firm's books and records by opening an account and signing a new account card, a Form W-9, and a stock power under an assumed name. According to the findings, Lipman endorsed a check made payable to this assumed name, and deposited the proceeds in his own bank account. The findings also stated that he opened an account at a member firm without notifying it of his association with another member firm.

Lipman's suspension commenced with the opening of business on April 19, 1993, and will conclude at the close of business May 18, 1993.

Jamie M. Lyles (Registered Representative, Birdsboro, Pennsylvania) was fined \$30,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Lyles forged signatures of customers on applications for variable life insurance policies and related forms and submitted such documents to his member firm. In addition, Lyles failed to respond to NASD requests for information.

Kelly M. Madigan (Registered Representative, Troy, New York) was fined \$10,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that, without the knowledge or consent of an insurance customer, Madigan submitted a false insurance surrender form and a fictitious new-policy application by forging the customer's signature. In addition, Madigan failed to respond to NASD requests for information.

Paul Z. Makris (Registered Representative, Fayetteville, Arkansas) was fined \$20,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions

following an appeal of a District 5 DBCC decision. The sanctions were based on findings that Makris made unauthorized withdrawals totaling \$8,690 from the account of a private club in which he maintained an ownership interest and converted the funds to his own use and benefit without the knowledge or consent of the club members. Makris changed the mailing address listed on the club's account to his home address so that other club members would not receive confirmations or account statements reflecting the unauthorized withdrawals.

Makris has appealed this action to the SEC, and the sanctions, other than the bar, are not in effect pending consideration of the appeal.

Charles Clifton Marshall (Registered Representative, Shawnee Mission, Kansas) was fined \$68,705.05, barred from association with any NASD member in any capacity, and required to pay \$13,741.01 in restitution to public customers. The sanctions were based on findings that, without the knowledge or consent of nine insurance customers, Marshall requested a withdrawal of dividends or surrender of paid-up insurance on their insurance policies and converted the proceeds therefrom to his own use and benefit.

Sheldon Maschler (Registered Representative, Bayonne, New Jersey) was fined \$5,000 and suspended from association with any NASD member in any capacity for one business day. The sanctions were based on findings that, on several occasions, Maschler used language that was indecorous and abusive while addressing persons associated with different member firms.

Deborah B. McLaughlin

(Registered Representative, Bridgeport, Connecticut) was fined \$50,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that McLaughlin participated in private securities transactions without providing prior written notification to her member firm. In addition, McLaughlin failed to respond to NASD requests for information.

George W. Moffitt, Jr. (Registered Principal, Philadelphia, Pennsylvania) submitted an Offer of Settlement pursuant to which he was fined \$2,500, jointly and severally with a member firm and barred from association with any NASD member in any principal, supervisory, or managerial capacity. In addition, Moffitt is precluded from having a proprietary interest in any broker/dealer. However, he may maintain a noncontrolling interest in a member whose stock is publicly traded and subject to the reporting requirements of Section 12(g) of the Securities Exchange Act of 1934.

Without admitting or denying the allegations, Moffitt consented to the described sanctions and to the entry of findings that a member firm, acting through Moffitt, tendered notes in the principal amount of \$80,000 held in a public customer's account without the customer's consent, failed to inform the customer of the true status of his securities account, and caused the customer to believe that he still owned certain securities until a later date.

In addition, the firm, acting through Moffitt, failed to notify the NASD of its change of exemption status or to obtain prior written approval from the NASD to engage in operations or activities that disqualified it from continued exemption under

the SEC Customer Protection Rule 15c3-3. Specifically, the findings stated that the firm, acting through Moffitt, failed to establish and maintain a Special Reserve Bank Account for the Exclusive Benefit of Customers, to make monthly computations of the amount required to be on deposit in the reserve account, and to make deposits to and maintain in the reserve account cash and qualified securities in the required amounts. The NASD also determined that the firm, acting through Moffitt, prepared an inaccurate net capital computation, filed inaccurate FOCUS Part I reports and failed to prepare and keep current books and records, including records of securities holdings.

In a separate action, Moffitt submitted a Letter of Acceptance, Waiver and Consent pursuant to which he consented to the sanctions set forth in the aforementioned Offer of Settlement. Without admitting or denying the allegations, Moffitt consented to these sanctions and to the entry of findings that the same member firm, acting through Moffitt, held customer securities, failed to prepare and maintain an accurate stock record, to prepare a blotter, or to maintain other sufficient records reflecting receipts and deliveries of securities. Moreover, the findings stated that the firm, acting through Moffitt, failed to prepare a record reflecting dividends and interest received, to prepare a complete and accurate record reflecting securities in transfer, and to conduct a required quarterly securities count.

Frank J. Neal (Registered Representative, Howell, New Jersey) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$33,300 and barred from association with any NASD member in

any capacity. Without admitting or denying the allegations, Neal consented to the described sanctions and to the entry of findings that he misappropriated for his own use \$14,040.13 from the accounts of public customers without their knowledge or consent.

Frank A. Nicolais (Registered Representative, Staten Island, New York) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Nicolais failed to provide testimony or to respond to NASD requests for information concerning transactions and activities in which he was involved while employed at a member firm.

Steven Joseph Nori (Registered Representative, Colma, California) was fined \$5,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Nori, on two occasions, effected a computer entry which created fictitious deposits totaling \$10,000 to his personal account.

James T. Ogle, II (Registered Representative, East Hartford, Connecticut) was fined \$40,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Ogle misappropriated to his own use and benefit customer funds totaling \$12,500 without the knowledge or consent of the customer. In addition, Ogle failed to respond to NASD requests for information.

Everett Gary Oliver (Registered Representative, North Mankato, Minnesota) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000 and suspended from association with any NASD member in

any capacity for 30 days. Without admitting or denying the allegations, Oliver consented to the described sanctions and to the entry of findings that he received the equivalent of \$9,700 in cash and goods from public customers in connection with purchases of annuities. The findings stated that he received these benefits by misrepresenting to the customers that the amounts were due for commissions and consulting fees, when these fees were included in the premium amount.

Eric C. Pietranton (Registered Representative, New Cumberland, West Virginia) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Pietranton failed to respond to NASD requests for information regarding his alleged failure to process customer funds and checks received by his member firm on a timely basis.

Anthony R. Raucci, Jr. (Registered Representative, Southington, Connecticut) was fined \$100,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that, without the knowledge or consent of his member firm or a public customer, Raucci misappropriated to his own use and benefit customer funds totaling \$38,257.50, intended for deposit into various tax-sheltered annuities. In addition, Raucci failed to respond to NASD requests for information.

Gerald Lee Reichenbacher (Registered Representative, Mesa, Arizona) was fined \$100,000 and barred from association with any NASD member in any capacity. In addition, Reichenbacher must pay \$160,433

in restitution to his former member firm plus interest at 9 1/2 percent from September 25, 1989, until paid. The sanctions were based on findings that Reichenbacher misused customer funds in that he withdrew, or caused to be withdrawn, \$160,435 from the bank accounts of a public customer without her knowledge or authorization.

Steven Farley Richards (Registered Representative, Aptos, California) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Richards consented to the described sanctions and to the entry of findings that he recommended and effected unsuitable transactions in the accounts of customers. In connection with such activity, the NASD found that Richards participated in private securities transactions without giving prior written notification to his member firm.

William H. Rookstool, III (Registered Representative, Doylestown, Pennsylvania) submitted an Offer of Settlement pursuant to which he was fined \$2,500 and suspended from association with any NASD member in any capacity for one month. Without admitting or denying the allegations, Rookstool consented to the described sanctions and to the entry of findings that he forged an insurance customer's signature on an application for reinstatement of a life insurance policy. The findings also stated that he forged another individual's signature on a form requesting the withdrawal of \$200 in accumulated policy dividends and submitted these documents to his member firm. The NASD determined that Rookstool used the funds to pay overdue premiums and

to reinstate the first customer's life insurance policy.

Anthony John Salemme (Registered Representative, Stockton, California) was fined \$37,650 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Salemme purchased and sold securities in the account of two public customers without their knowledge and consent. Salemme also failed to respond to NASD requests for information.

Peter W. Schellenbach (Registered Principal, Glencoe, Illinois) was fined \$50,000, jointly and severally with a former member firm. In addition, he was suspended from association with any NASD member in any capacity for 60 days, barred in any principal, supervisory, or managerial capacity, and prohibited from maintaining any proprietary interest in any non-publicly traded member of the NASD.

The United States Court of Appeals for the Seventh Circuit affirmed the action following an appeal of an SEC decision. The sanctions were based on findings that a former member firm, acting through Schellenbach, failed to prepare and maintain accurate books and records, effected securities transactions when it failed to maintain its minimum required net capital, prepared and filed inaccurate FOCUS Part I and IIA reports, filed its annual audited report late for one year, and failed to file its financial statements the following year.

Furthermore, Schellenbach engaged in a pattern of activity designed to give the illusion that the firm was in compliance with net capital requirements by engaging in the month-end purchase and subsequent resale of accounts receivable of the firm

on four separate occasions. In addition, the firm, acting through Schellenbach, failed to establish, maintain, and enforce adequate written supervisory procedures and failed to review and provide evidence of approval in writing on all correspondence of its registered representatives pertaining to the solicitation or execution of securities transactions.

Thomas H. Schneider (Registered Representative, McMurray, Pennsylvania) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Schneider failed to respond to NASD requests for information.

Billy Lawrence Simpson (Registered Representative, Wheaton, Illinois) was fined \$54,000, barred from association with any NASD member in any capacity, and ordered to pay \$14,000 in restitution to a customer. The fine may be reduced by any amount of restitution paid to the customer (reduction not to exceed \$4,651.59). The NBCC imposed the sanctions following an appeal of a District 8 DBCC decision. The sanctions were based on findings that Simpson obtained from a public customer a \$14,000 check with instructions to invest \$9,000 in a municipal bond fund and \$5,000 in a high yield investment. Contrary to the customer's instruction, and without her knowledge or consent, Simpson failed to invest the \$14,000 and, instead, retained the funds for his own use and benefit.

Avinash M. Suchak (Registered Representative, Middlesex, United Kingdom) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$100,000 and barred from association with any NASD mem-

ber in any capacity. Without admitting or denying the allegations, Suchak consented to the described sanctions and to the entry of findings that he executed numerous purchases and sales of futures contracts in the account of a public customer without the customer's authorization.

William K. Tingley (Registered Representative, Ansonia, Connecticut) was fined \$10,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Tingley misappropriated to his own use and benefit customer funds totaling \$451 intended for insurance premium payments. In addition, Tingley failed to respond to NASD requests for information.

Bradley L. Uhlfelder (Registered Representative, Owings Mills, Maryland) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Uhlfelder failed to respond to NASD requests for information concerning several customer complaints.

Robert Arnold Wald (Registered Representative, St. Louis, Missouri) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 30 days. The suspension will continue thereafter until restitution of \$12,030 plus interest is paid to public customers. Without admitting or denying the allegations, Wald consented to the described sanctions and to the entry of findings that he recommended and executed transactions in the accounts of public customers without having reasonable grounds for believing that the recommendations were suitable in light of the

nature, size, and frequency of the recommended transactions and the customers' investment objectives, financial situations, and needs.

David A. Wallace (Registered Representative, Sarasota, Florida) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$2,500, suspended from association with any NASD member in any capacity for two business days, and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Wallace consented to the described sanctions and to the entry of findings that he recommended that a public customer engage in short-term trading of equity securities on margin. The NASD found that this recommendation was unsuitable.

J. Robert Wilgus (Registered Representative, Duluth, Georgia) was barred from association with any NASD member in any capacity. The sanction was based on findings that Wilgus exercised discretionary power in non-discretionary accounts of public customers. Wilgus also recommended and executed securities transactions in the custodial account of a public customer without having reasonable grounds for believing that such transactions were suitable for the customer.

In addition, Wilgus obtained \$20,000 from the securities account of a public customer for investment purposes and, by transmitting the funds to his personal bank account, and thereafter converted the monies to his own use and benefit without the customer's knowledge or consent.

Michael C. Williams (Registered Representative, Augusta,

Georgia) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000 and suspended from association with any NASD member in any capacity for six months.

Without admitting or denying the allegations, Williams consented to the described sanctions and to the entry of findings that, without the knowledge or authorization of a public customer, he withdrew \$22,500 from the customer's checking account and used the funds to pay administrative costs and personal expenses.

Stephen Wolfson (Registered Representative, Revere, Massachusetts) was fined \$60,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Wolfson misappropriated to his own use and benefit \$28,623 in customer funds intended for the purchase of a life insurance policy without the customer's knowledge or consent. In addition, Wolfson failed to respond to NASD requests for information.

Michael Charles Woloshin (Registered Representative, New York, New York) and **Stewart Emanuel Holzkenner (Registered Representative, New York, New York)** submitted an Offer of Settlement pursuant to which Woloshin was fined \$20,000 and suspended from association with any NASD member in any capacity for 14 days. Holzkenner was fined \$2,500, suspended from association with any NASD member in any capacity for 10 business days, and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that, on several occasions, they purchased from an individual at

another member firm microfiche reflecting customer account information of the firm.

Individuals Fined

Carlos Alberto Enriquez (Registered Principal, Coral Gables, Florida) submitted an Offer of Settlement pursuant to which he was fined \$14,400. Without admitting or denying the allegations, Enriquez consented to the described sanction and to the entry of findings that, in contravention of the Board Of Governors' Free-Riding and Withholding Interpretation, Enriquez purchased shares of a "hot issue."

Zachary S. Hanoyan (Registered Representative, Boston, Massachusetts) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$12,000 and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Hanoyan consented to the described sanctions and to the entry of findings that he recommended and executed purchase and sale transactions in the account of a public customer with undue frequency and without reasonable justification.

Frederick C. Heller (Registered Representative, Englewood, Colorado) was fined \$12,500. The SEC affirmed the sanction following an appeal of a August 1991 NBCC decision. The sanction was based on findings that Heller effected excessive transactions in the account of public customers in view of the resources and nature of the customers' account and of their investment objectives and exercised discretion in the same account without obtaining written discretionary trading authority from these customers or his member firm.

David A. Ledden (Registered Representative, Aurora, Colorado) was fined \$10,000 and required to requalify by examination. The sanctions were based on findings that Ledden sent correspondence to a public customer that overstated the value of certain securities owned by the customer. In addition, Ledden failed to follow his member firm's written supervisory procedures in that he sent the aforementioned correspondence and other related material to the customer without obtaining the prior approval of his manager.

George William Scherzer (Registered Representative, Portland, Oregon) submitted an Offer of Settlement pursuant to which he was fined \$10,000 and required to requalify by examination as a general securities representative. Without admitting or denying the allegations, Scherzer consented to the described sanctions and to the entry of findings that he exercised discretion in a customer's account without obtaining prior written discretionary trading authority. The findings also stated that Scherzer recommended unsuitable transactions in the same customer's account.

Robert W. Weed (Registered Representative, Wilson, Wyoming) was fined \$10,000. The sanction was based on findings that Weed recommended to public customers the purchase of securities without having reasonable grounds for believing that these recommendations were suitable considering the customers' investment objectives, financial situations, and needs.

Firms Expelled for Failure to Pay Fines and Costs in Connection With Violations

FirstMoney Securities Corporation, Memphis, Tennessee

Meritquest Group, Incorporated, Glendale, California

Peckskamp & Company, Incorporated, Cincinnati, Ohio

Individuals Whose Registrations Were Revoked for Failure to Pay Fines and Costs in Connection With Violations

James L. Begbie, Denver, Colorado

Keith A. Bergner, Lakewood, Colorado

David A. Bohnenkamper, Palm Harbor, Florida

Richard J. Calta, Phoenix, Arizona

John J. Cox, Denver, Colorado

Albert F. DeMange, Coral Springs, Florida

Robert L. Eaton, Kingsport, Tennessee

Thomas S. Foti, Tucson, Arizona

Michael A. Iwe, Jr., Chicago, Illinois

Kim H. Johnson, Sandy, Utah

Donald W. Jones, Renton, Washington

Peter K. Lloyd, Odessa, Florida

Paul D. Melvey, Fargo, North Dakota

Kevin J. Sakser, Marietta, Georgia

Andrew L. Scudiero, Whitestone, New York

Thomas R. Sparks, Sr., Scottsdale, Arizona

Martin B. Wewerka, El Cajon, California

NASD Announces Two Significant Disciplinary Actions

The NASD has taken action against Pacific Southern Securities, Inc., formerly a member firm located in Denver Colorado; Gerald M. Schechter of Englewood, Colorado; William P. Snow, Sr., of Arvada, Colorado; Edgel G. Groves of Atlanta, Georgia; and, Paul D. Melvey of Fargo, North Dakota. Pursuant to an Offer of Settlement which neither admitted nor denied the allegations contained in the Complaint, the firm was fined \$800,000, jointly and severally with Schechter and Snow, and expelled from NASD membership. In addition, Schechter and Snow were barred from associating with any NASD member in any capacity. Groves was fined \$150,000 and suspended from association with any NASD member in any capacity for two years. Melvey was fined \$2,500 and suspended from association with any NASD member in any capacity for four years.

All four individuals were associated with Pacific Southern. Schechter served as the firm's President and head trader, Snow was responsible for corporate financing, Groves was responsible for the operations of the firm's franchise branch office located in Atlanta, Georgia, and Melvey was responsible for assisting in the preparation of a newsletter prepared by the firm.

The complaint charged that the firm, Schechter, Snow, and Groves employed manipulative, deceptive, and other fraudulent devices in 1989 through 1991 in the purchase

and sale of Vintage Capital Corp. securities (Vintage), a penny stock which traded over-the-counter.

Pacific Southern underwrote Vintage, a blind pool, and placed 100 percent of the offering with its own customers. Thereafter, Schechter and Snow continually recommended the purchase of Vintage in the face of known material adverse information. Both knew that the price rise in Vintage from \$.01 to over \$.10 per share was arbitrarily determined by the firm and Schechter, was unsupported by market demand or corporate developments, and the Pacific Southern dominated and controlled the after-market trading in Vintage.

The Decision Accepting Offers of Settlement stated that Schechter and Snow were the “master minds and major participants in the Vintage manipulation,” and Snow acted as an undisclosed promoter and control person of Vintage and the firm. As a result of this misconduct, the firm reaped profits of over \$600,000. Groves, as the franchise branch owner, was responsible for the sale of the majority of Vintage common stock and warrants. He continued to recommend and sell Vintage to customers in the absence of material information about the company. For his part, Melvey assisted in issuing materially misleading newsletters to the public.

The NASD also took disciplinary action against a Minneapolis broker, William C. Murphy; John G. Kinnard & Co., Inc., a member firm; and five other individuals for various violations of the Association’s rules.

Pursuant to an Offer of Settlement,

in which he neither admitted nor denied the allegations set forth in the NASD’s Complaint, Murphy was fined \$100,000 and permanently barred from associating with any member firm in any capacity. According to the NASD, between 1985 and 1989 Murphy, while employed as a registered representative of John G. Kinnard & Co., Inc., established several brokerage accounts in other people’s names, both at Kinnard and at other Minneapolis broker/dealers. He then actively traded in the accounts, without authority, for his personal gain. In doing so, Murphy falsified new account information and forged customer signatures so as to conceal his true interest in, and control of, these nominee accounts. Murphy was also sanctioned for his refusal to cooperate with the NASD in its investigation of his activities.

Murphy’s former employer, John G. Kinnard & Co., Inc.; the firm’s Executive Vice President, Plato A. Mavroulis; and Chief Compliance Officer, Gerald M. Gifford, also settled with the NASD without admitting or denying the allegations. The NASD found that Kinnard, Mavroulis, and Gifford failed adequately to supervise Murphy, and failed to conduct an adequate review of his activities once his misconduct was brought to their attention. As a result, Kinnard, Mavroulis, and Gifford were fined \$35,000, jointly and severally. Mavroulis and Gifford were also suspended for three business days in all capacities, and the firm agreed to hire an independent consultant to conduct a thorough review of its supervisory policies, procedures, and practices.

The NASD also accepted Offers of

Settlement from Alex P. Karos and Daniel L. Rhode, who also neither admitted nor denied the allegations made against them. According to the NASD, Karos, who was associated with another Minneapolis brokerage firm, assisted Murphy in establishing two nominee accounts, and then knowingly executed numerous unauthorized trades on his behalf, without first notifying his own member firm. Rhode, who was associated with a third Minneapolis firm, also assisted Murphy in opening a nominee account, and knowingly effected unauthorized trades for him, without first notifying his own member firm. As a result, Karos was fined \$40,000, suspended for three months in all capacities, and prohibited from maintaining any retail customers accounts. Rhode was fined \$7,500 and suspended for two months in all capacities.

Murphy’s nephew, Coley D. Murphy, settled with the NASD without admitting or denying allegations that he had refused to cooperate with the Association’s investigation. At the time, Coley Murphy was associated with a fourth Minneapolis broker/dealer. As a result, he was fined \$10,000 and suspended for two years in all capacities.

The NASD’s investigations were carried out by its Anti-Fraud Department in Washington, DC. The action relating to Pacific Southern is part of a continuous nationwide effort by the NASD to eliminate trading and sales-practice abuses in penny stocks. The NASD and Minnesota Department of Commerce, Enforcement Division, worked cooperatively in the matter relating to John G. Kinnard.

FOR YOUR INFORMATION

Arkansas Increases Agent Registration, Re-Registration, and Renewal Fees

On April 7, 1993, Arkansas authorized the CRD to begin collecting agent registration, re-registration, and renewal fees of \$75. This is an increase from the current \$50 fee. Firm registration and renewal fees will remain at \$300. If you have any questions regarding these changes, please call the Arkansas Securities Department at (501) 324-9260.

Paper and Pencil Series 7 Available in Spokane, Washington June 5

Effective June 5, 1993, candidates may take the General Securities Representative Examination (Series 7) at the Paper & Pencil Examination Center (Center) in Spokane, Washington, on the first Saturday of each month. In addition to the Spokane Center, candidates may take the Series 7 at the Centers in Anchorage, Alaska; Honolulu, Hawaii; and Great Falls, Montana.

To take the Series 7 examination at one of these locations, candidates must make an appointment by telephoning the NASD Member Services Phone Center in Rockville, Maryland at (301) 590-6500.

Appointments must be made with the NASD eight business days before the desired examination session.

Examination Revisions Announced

Effective July 1, 1993, some NASD examinations will reflect various recently implemented NASD and SEC rule changes. Please note that these changes will affect only the examinations that currently cover these rules.

- The Net Capital Rules (SEC Rule 15c3-1) — the changes to the minimum net capital requirements, by class of broker/dealer, effective July 1 to December 31, 1993, as well as amendments to the securities haircuts, aggregate indebtedness, and contractual charges (refer to *Notice to Members 92-72*).
- The small issue exemption from the registration requirements of the Securities Act of 1933 under Regulation A.
- NASD Rules of Fair Practice — Section 10 (refer to *Notice to Members 93-8*); Section 35 (refer to *Notice to Members 93-18*); and Section 45 (refer to *Notice to Members 92-60*).

For further explanation, contact Carole Hartzog at (301) 590-6696.

NASD NOTICE TO MEMBERS 93-35

Mail Vote — Proposed Amendment to the Procedures for Filling Vacancies on NASD® Nominating Committees; Last Voting Date: July 26, 1993

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD® invites members to vote on a proposed amendment to Article IX, Section 4 of the NASD By-Laws to conform the procedures for filling vacancies on Nominating Committees to those currently in place for District Committees. The change would eliminate the requirement for special elections to fill vacancies where more than six months remain in the unexpired term. **The last voting date is July 26, 1993.** The text of the amendment follows this Notice.

Background and Description of Proposal

The NASD By-Laws currently provide different procedures for filling vacancies on a District Nominating Committee and a District Committee. Article IX, Section 4 of the By-Laws provides that Nominating Committee vacancies caused by other than the expiration of a member's term of office shall be filled by appointment by the remaining members of the Nominating Committee if the unexpired term is for less than six months, but that if the unexpired term is for six months or more, such vacancy shall be filled by special election. Article VIII, Section 5 of the By-Laws relating to the filling of vacancies on District Committees, however, provides that the District Committee shall appoint a representative of a member firm having a place of business in the District to fill any vacancy resulting from the unexpired term of a departed committee member and that such appointment shall be effective until the next regularly scheduled election.

Request for Vote

The Board of Governors believes

that the special election provision for Nominating Committee vacancies serves no valid purpose and is a costly and cumbersome mechanism, particularly in view of the fact that the term of Nominating Committee members is only one year. Accordingly, the Board of Governors is proposing to amend Article IX, Section 4 of the By-Laws to provide for the same procedures to be used in filling Nominating Committee vacancies as are used to fill District Committee vacancies. The proposed rule change provides that any Nominating Committee shall appoint a representative of a member of the NASD eligible to vote in the same District to fill a vacancy until the next regularly scheduled election. The Board considers the proposed rule change necessary and appropriate and recommends that members vote their approval. Please mark the attached ballot according to your convictions and mail in the enclosed, stamped envelope to The Corporation Trust Company. Ballots must be postmarked **no later than July 26, 1993.** Questions concerning this Notice should be directed to Elliott R. Curzon, Office of General Counsel, at (202) 728-8451.

Text of Proposed Amendment To Article IX, Section 4 of the By-Laws

(Note: New text is underlined; deleted text is in brackets.)

Filling of Vacancies for Nominating Committees

Sec. 4. [All vacancies in any Nominating Committee other than those caused by the expiration of a member's term of office shall be filled as follows:]

[(a) If the unexpired term of the

member causing the vacancy is for less than six months, such vacancy shall be filled by appointment by the remaining members of the Nominating Committee of a representative of a member of the Corporation eligible to vote in the same District.]

[(b) If the unexpired term of the member causing the vacancy is for

six months or more, such vacancy shall be filled by election, which shall be conducted as nearly as practicable in accordance with the provisions of Section 3 of this Article.]

In the event of any vacancy on any Nominating Committee caused by the departure of a Committee member prior to the expiration of that

member's term of office the Nominating Committee shall appoint a representative of a member of the Corporation eligible to vote in the same District to fill the vacancy. Such appointment shall be effective until the next regularly scheduled election occurs, in accordance with the provisions of Section 3 of this Article.

NASD NOTICE TO MEMBERS 93-36

Codification of Investment Company Advertising Guidelines

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On April 30, 1993, the Securities and Exchange Commission (SEC) approved an amendment to Article III, Section 35 of the Rules of Fair Practice and the Investment Company Securities section of the *NASD Manual*. The amendment adds language relating to investment companies to Article III, Section 35 of the Rules of Fair Practice, as set forth below, and deletes the *Guidelines Regarding Communications With the Public About Investment Companies and Variable Contracts* published at ¶5286 of the *NASD Manual*. The amendments are effective July 1, 1993. The text of the amendments follows this Notice.

Background

On April 30, 1993, the SEC approved an amendment to the NASD's rules codifying several of the *Guidelines Regarding Communications With the Public About Investment Companies and Variable Contracts* published at ¶5286 of the *NASD Manual* (*Guidelines*). The amendment deletes the *Guidelines* and amends Article III, Section 35 of the Rules of Fair Practice.

The *Guidelines* were adopted by the NASD® in 1982 following the SEC's 1979 repeal of its Statement of Policy on Investment Company Sales Literature and are set forth at ¶5286 of the *NASD Manual*. When the SEC amended Rule 482 under the Securities Act of 1933 and Rule 34b-1 under the Investment Company Act of 1940 relating to the communication of investment company performance to the public, many of the provisions of the *Guidelines* were rendered obsolete.

Accordingly, in the amendment

approved by the SEC, the NASD has rescinded the *Guidelines* and amended Article III, Section 35 of the Rules of Fair Practice by adding those provisions of the *Guidelines* that imposed general standards for communications and certain specific standards for communications concerning claims of tax free or tax exempt returns, comparisons, and predictions and projections. The amended provisions apply to advertisements for all types of investments, while the *Guidelines* applied only to investment company and variable contract products.

New Subsection 35(d)(1)(D) incorporates the entire provision set forth as "General Considerations," currently included in the first section of the *Guidelines*, under the Section 35 provision that imposes general "Standards Applicable to Communications With the Public." The first standard under new paragraph 35(d)(1)(D)(i) relates to the overall context of a statement and requires members to consider that a statement may be misleading in one context while being perfectly appropriate in another context. The principal test of this standard is whether the statement adequately balances the potential risks with the potential benefits. This provision is identical to the language currently contained in the *Guidelines*.

The standard set forth in new paragraph 35(d)(1)(D)(ii) relates to the importance of the target audience as a factor in evaluating the communication. The provision requires varying levels of explanation or detail in a communication depending on the audience and the member's ability to restrict the communication to the intended audience. Members are required to consider the likelihood that the communication could be received by persons for whom the explanations or information are inadequate or misleading. This

provision incorporates rule language identical to that currently contained in the *Guidelines*.

The standard set forth in new paragraph 35(d)(1)(D)(iii) requires all statements in communications to be made clearly and cautions against complex or overly technical explanations, and the inclusion of material information in legends or footnotes. This provision incorporates rule language identical to that currently contained in the *Guidelines*.

New Subsections 35(d)(2)(L), (M), and (N) incorporate a number of concepts contained in other parts of the *Guidelines* into the requirements set forth as “Specific Standards” for communications with the public in Section 35. Subsection 35(d)(2)(L) prohibits members from stating that an investment is “tax free” or “tax exempt” if income tax liability is merely postponed or deferred, and requires that if there are references to tax free/tax exempt current income or if income taxes are payable on redemption, those facts and any applicable income taxes must be adequately disclosed. The rule language of this provision is drawn from the last paragraph of the section in the *Guidelines* titled “4. Specific Considerations in Presenting Yield Data or Illustrations.”

Subsection 35(d)(2)(M) requires members, when using comparisons, to ensure that the comparisons are clear, fair, balanced, and include any material differences between the subjects of the comparison such as liquidity, safety, investment objectives, and fees, among others. The rule language of this provision is drawn from the first three paragraphs of the section in the *Guidelines* titled “5. Considerations Regarding Comparisons.”

Subsection 35(d)(2)(N) prohibits members from predicting or projecting future performance on any basis, including past performance. Hypothetical illustrations of mathematical principles such as dollar cost averaging, however, are not considered projections of performance. The rule language of this provision is based on that included in the section in the *Guidelines* titled “Adequacy of Information Concerning the Relevance of Results Illustrated to Probable Future Results.”

The amendments are effective July 1, 1993. Questions concerning this Notice may be directed to the NASD’s Advertising Regulation Department at (202) 728-8330, or to Elliott R. Curzon, Senior Attorney, Office of General Counsel, (202) 728-8451.

Text of Amendment to Article III, Section 35 of the Rules of Fair Practice

(Note: New text is underlined.)

Communications With the Public Sec. 35.

* * * * *

(d) Standards Applicable to Communications With the Public

(1) General Standards

* * * * *

(D) In judging whether a communication or a particular element of a communication may be misleading, several factors should be considered, including but not limited to:

(i) The Overall Context in Which the Statement or Statements Are Made: A statement made in one

context may be misleading even though such a statement could be perfectly appropriate in another context. An essential test in this regard is the balance of treatment of risks and potential benefits.

(ii) The Audience to Which the Communication Is Directed: Different levels of explanation or detail may be necessary depending on the audience to which a communication is directed, and the ability of the member given the nature of the media used, to restrict the audience appropriately. If the statements made in a communication would be applicable only to a limited audience, or if additional information might be necessary for other audiences, it should be kept in mind that it is not always possible to restrict the readership of a particular communication.

(iii) The Overall Clarity of the Communication: A statement or disclosure made in an unclear manner obviously can result in a lack of understanding of the statement, or in a serious misunderstanding. A complex or overly technical explanation may be worse than too little information. Likewise material disclosure relegated to legends or footnotes realistically may not enhance the reader’s understanding of the communication.

(2) Specific Standards

In addition to the foregoing general standards, the following specific standards apply:

* * * * *

(L) Claims of Tax Free/Tax Exempt Returns: Income or investment returns may not be characterized as tax free or exempt from income tax where tax liability is merely postponed or deferred. If taxes are payable upon redemption, that fact

must be disclosed. References to tax free/tax exempt current income must indicate which income taxes apply or which do not unless income is free from all applicable taxes. For example, if income from an investment company investing in municipal bonds may be subject to state or local income taxes, this should be stated, or the illustration should otherwise make it clear that income is free from federal income tax.

(M) Comparisons: In making a comparison, either directly or indi-

rectly, the member must make certain that the purpose of the comparison is clear and must provide a fair and balanced presentation, including any material differences between the subjects of comparison. Such differences may include investment objectives, sales and management fees, liquidity, safety, guarantees or insurance, fluctuation of principal and/or return, tax features, and any other factors necessary to make such comparisons fair and not misleading.

(N) Predictions and Projections:

Investment results cannot be predicted or projected. Investment performance illustrations may not imply that gain or income realized in the past will be repeated in the future. However, for purposes of this rule, the following types of information are not considered projections of performance; hypothetical illustrations of mathematical principles, (e.g., illustrations designed to show the effects of dollar cost averaging, tax-free compounding, or the mechanics of variable annuity contracts or variable life policies).

NASD NOTICE TO MEMBERS 93-37

NASD® Expands the Public Disclosure Program

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

On January 18, 1993, the NASD's Board amended its Public Disclosure Program to make additional regulatory information on its members and associated persons available to the public. The Board's action will expand this program to include civil judgments and NASD arbitration decisions involving securities matters, pending regulatory actions, and criminal indictments and informations. Previously, only criminal convictions and final disciplinary actions taken by self-regulatory organizations (SROs) and federal or state securities agencies were available. Implementation of the disclosure program enhancements will be in two stages with the first stage scheduled for July 1, 1993. The public disclosure hotline may be reached toll-free at (800) 289-9999.

Background

On May 3, 1988, the NASD® established a Public Disclosure Program that permits certain types of disciplinary information on NASD member firms and associated persons to be available to the public. This program provides investors with access to information on an NASD member or any of the member's associated persons with whom the customer might transact business. At startup, the program allowed for the release of final disciplinary action(s) taken by SROs or federal or state securities agencies that relate to securities or commodities transactions; as well as criminal convictions. The information was released to the public upon receipt of a written request.

On October 1, 1991, the NASD made further improvements to the program when it established a toll-free number for investors to use

when requesting this information.

Public Disclosure of Arbitration Awards

In May 1989, as a result of an SEC requirement, the NASD implemented a program separate from the Public Disclosure Program that made final NASD arbitration decisions (awards) issued after that date in public customer cases publicly available.

Enhancement of the Public Disclosure Program

As a result of recent action by the NASD Board, the Public Disclosure Program will now include civil judgments and NASD arbitration decisions involving securities matters; pending formal disciplinary proceedings initiated by the NASD, SEC, state securities administrators, and other SROs; and criminal indictments and informations. The NASD will link the data bases that contain disciplinary actions and NASD arbitration awards to ensure proper disclosure of such data on industry forms as well as to facilitate public access to all disclosable information through a single toll-free number. Member firms should inform their associated persons of the expansion of the Public Disclosure Program to make them aware of the information available to the public regarding their background and their disciplinary record in the industry. This notification is especially important since the program is gaining more public awareness. Information relating to the NASD's Public Disclosure Program was widely circulated in a press release on January 19, 1993, and has since been the subject of a number of newspaper and magazine articles. Also, with the adoption of Rule 15g-2 under "The Penny

Stock Reform Act,” certain member firms are required to make available a risk disclosure document, describing the availability of the toll-free telephone number, to all their investors and prospective investors.

Implementation Schedule

NASD arbitration awards for the

period of May 10, 1989, to August 6, 1990, will not be available in the first implementation phase beginning July 1, 1993. This information is now being gathered and will be available for disclosure on September 1, 1993.

The Public Disclosure Program service is free to investors. However, the program charges \$30 per

inquiry for law firms, banks, and any other commercial callers. Member firms can receive the Public Disclosure Program information through the Firm Access Query System (FAQS) by using the “PREHIRE” command.

For questions relating to this Notice, call the Member Services Phone Center at (301) 590-6500.

NASD NOTICE TO MEMBERS 93-38

Independence Day: Trade Date-Settlement Date Schedule

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

The Nasdaq Stock MarketSM and the securities exchanges will be closed on Monday, July 5, 1993 in observance of Independence Day. "Regular way" transactions made on the preceding business days will be subject to the settlement date schedule listed below.

<u>Trade Date</u>	<u>Settlement Date</u>	<u>Reg. T Date*</u>
June 25	July 2	July 7
28	6	8
29	7	9
30	8	12
July 1	9	13
2	12	14
5	Markets Closed	—
6	13	15

Brokers, dealers, and municipal securities dealers should use these settlement dates to clear and settle transactions pursuant to the NASD[®] Uniform Practice Code and Municipal Securities Rulemaking Board Rule G-12 on Uniform Practice.

Questions regarding the application of these settlement dates to a particular situation may be directed to the NASD Uniform Practice Department at (212) 858-4341.

*Pursuant to Sections 220.8(b)(1) and (4) of Regulation T of the Federal Reserve Board, a broker/dealer must promptly cancel or otherwise liquidate a customer purchase transaction in a cash account if full payment is not received within seven (7) business days of the date of purchase or, pursuant to Section 220.8(d)(1), make application to extend the time period specified. The date by which members must take such action is shown in the column entitled "Reg. T Date."

NASD NOTICE TO MEMBERS 93-39

As of May 24, 1993, the following 58 issues joined the Nasdaq National Market,[®] bringing the total number of issues to 3,108:

Nasdaq National Market[®]
Additions, Changes,
And Deletions as of
May 24, 1993

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Symbol	Company	Entry Date	SOES Execution Level
SFSW	State Financial Services Corporation	4/26/93	500
ACTNW	Action Performance Companies, Inc. (4/27/98 Wts)	4/27/93	500
ACTN	Action Performance Companies, Inc.	4/27/93	500
CPIA	CPI Aerostructures, Inc.	4/27/93	1000
CPIAW	CPI Aerostructures, Inc. (9/16/95 Wts)	4/27/93	1000
CTLI	CTL Credit, Inc.	4/28/93	1000
INLQ	INTERLINQ Software Corporation	4/28/93	1000
JBIL	Jabil Circuit, Inc.	4/29/93	500
OASI	Old America Stores, Inc.	4/29/93	1000
ABSO	Absolute Entertainment, Inc.	4/30/93	1000
BFOH	BancFirst Ohio Corp.	4/30/93	200
EAIN	Education Alternatives, Inc.	4/30/93	1000
ERSI	Electronic Retailing Systems International, Inc.	4/30/93	1000
FDNY	Fidelity New York F.S.B.	5/3/93	1000
SBIT	Summit Bancshares, Inc.	5/3/93	200
THDO	The 3DO Company	5/4/93	1000
CWKTF	Cam-Net Communications Network, Inc.	5/10/93	1000
AMTR	Amtran, Inc.	5/11/93	500
CSNO	Casino America, Inc.	5/11/93	1000
CATS	Catalyst Semiconductor, Inc.	5/11/93	200
EVGM	Evergreen Media Corporation (CI A)	5/11/93	500
JCFS	Jackson County Federal Bank, Federal Savings Bank	5/11/93	200
JCFSP	Jackson County Federal Bank, Federal Savings Bank (Ser A Pfd)	5/11/93	200
PKVL	Pikeville National Corporation	5/11/93	1000
TELR	Telor Ophthalmic Pharmaceuticals, Inc.	5/11/93	1000
AGCOZ	AGCO Corporation (Dep Shrs)	5/12/93	200
ASPX	Auspex Systems, Inc.	5/12/93	1000
QSYS	Quad Systems Corporation	5/12/93	200
BHWK	Black Hawk Gaming & Development Co., Inc.	5/13/93	500
BHWKW	Black Hawk Gaming & Development Co., Inc. (CI A Wts 12/31/94)	5/13/93	500
BHWKZ	Black Hawk Gaming & Development Co., Inc. (CI B Wts 6/30/96)	5/13/93	500
LCII	LCI International, Inc.	5/13/93	500
OPTI	OPTI, Inc.	5/13/93	1000
PKPSR	Poughkeepsie Savings Bank (The) FSB (Rts 6/15/93)	5/13/93	500
IRGT	IRG Technologies, Inc.	5/14/93	1000

Symbol	Company	Entry Date	SOES Execution Level
HMHC	Hallmark Healthcare Corporation (CI A)	5/17/93	500
PBCTP	People's Bank (Ser A Pfd)	5/17/93	500
DIYH	D.I.Y. Home Warehouse, Inc.	5/18/93	1000
GABC	GAB Bancorp	5/18/93	200
MTCC	Magnetic Technologies Corporation	5/18/93	1000
MEGT	Megatest Corporation	5/18/93	200
HOST	Amerihost Properties, Inc.	5/19/93	1000
PGSAY	Petroleum Geo-Services A/S (ADR)	5/19/93	1000
CWEI	Clayton Williams Energy, Inc.	5/20/93	1000
HARY	Harry's Farmers Market, Inc. (CI A)	5/20/93	1000
MFST	MFS Communications Company, Inc.	5/20/93	1000
NHCI	National Home Centers, Inc.	5/20/93	1000
PMRP	PMR Corporation	5/20/93	1000
TWII	Titan Wheel International, Inc.	5/20/93	1000
CHBC	Chattahoochee Bancorp, Inc.	5/21/93	1000
IVFAP	IVF America, Inc. (Ser A Pfd)	5/21/93	500
SCSWF	Stolt Comex Seaway S.A.	5/21/93	1000
SUPI	Supreme International Corporation	5/21/93	1000
TDCZV	Therapeutic Discovery Corporation/ALZA Corporation	5/21/93	1000
CATP	Cambridge Technology Partners, Inc.	5/24/93	1000
CLIN	CliniCom Incorporated	5/24/93	1000
DOVT	DOVatron International, Inc.	5/24/93	1000
IVFA	IVF America Inc.	5/24/93	1000

Nasdaq National Market Symbol and/or Name Changes

The following changes to the list of Nasdaq National Market securities occurred since April 24, 1993:

New/Old Symbol	New/Old Security	Date of Change
HEALW/HEALW	Healthwatch, Inc. (4/30/94 Wts)/Healthwatch, Inc. (4/30/93 Wts)	4/26/93
YELL/YELL	Yellow Corporation/Yellow Freight System, Inc. of Delaware	4/26/93
POBR/POEA	Poe & Brown, Inc./Poe & Associates, Inc.	4/29/93
CSFC/CSFCB	CSF Holdings, Inc./CSF Holdings, Inc. (CI B)	5/3/93
NATL/NATL	NAI Technologies, Inc./North Atlantic Industries, Inc.	5/3/93
WELS/CRIX	Wellstead Industries Inc./Control Resource Industries Inc.	5/14/93
NCELW/NCELW	Nationwide Cellular Service Inc. (6/1/93 Wts)/Nationwide Cellular Service Inc. (5/17/93 Wts)	5/17/93
INVS/INVS	Investors Bank Corp./Investors Savings Corp.	5/24/93

Nasdaq National Market Deletions

Symbol	Security	Date
SOSI	Sundowner Offshore Services, Inc.	4/27/93
CAFS	Cardinal Financial Group, Inc.	5/3/93
KEYC	Key Centurion Bancshares, Inc.	5/3/93

Symbol	Security	Date
BLRGZ	Blue Ridge Real Estate Co.-Big Boulder Corp. (Uts)	5/4/93
NORKZ	Norsk Data A.S. B (ADR)	5/4/93
NBIC	Northeast Bancorp, Inc.	5/4/93
FRFD	First Community Bancorp Inc.	5/7/93
SCIOW	Scios Nova Inc. (CL C Wts)	5/10/93
BRAN	The Brand Companies, Inc.	5/10/93
INAI	IntelliCorp, Inc.	5/12/93
CFSC	CFS Financial Corporation	5/14/93
HDVSW	H.D. Vest Inc. (5/21/93 Cl A Wts)	5/17/93
BIOPQ	Bioplasty, Inc.	5/19/93
GULL	Gull Laboratories, Inc.	5/20/93
RCHI	Ranch Industries, Inc.	5/24/93

Questions regarding this Notice should be directed to Mark A. Esposito, Supervisor, Market Listing Qualifications, at (202) 728-8002. Questions pertaining to trade reporting rules should be directed to Bernard Thompson, Assistant Director, NASD Market Surveillance, at (301) 590-6436.

BOARD BRIEFS

Actions Taken by the NASD[®] Board of Governors in May

• **President's Report** — Nasdaq[®] continues to turn in strong performances as average daily share volume in March came in at 247.1 million shares, with April recording a solid average daily share volume of 243.5 million shares. Although somewhat below the levels for January and February, both months remain significantly ahead of 1992's record 190.8 million average daily share volume. Total Nasdaq volume was 20.2 billion shares at the end of April, representing nearly 42 percent of 1992's all-time record of 48.5 billion shares. In addition, the number of market makers, 491, and market-maker positions, 54,200, as well as the number of market makers per security, 11.6, have hit new highs. As expected from the surge in trading activity, all Nasdaq trading services have increased, with 1993's Small Order Execution System (SOES)SM volume up 70 percent over 1992; SelectNetSM volume up 37 percent; and the Advanced Computerized Execution System (ACES)[®] volume up 31 percent.

Internationally, there has been increasing interest among overseas markets and market participants in developing or acquiring systems to facilitate screen-based dealer markets. The President briefed the Board on several negotiations actively underway.

The NASD's International Markets Advisory Board (IMAB) met recently in Paris. During its meeting, the IMAB covered a number of general issues, including the regulatory environment for future global financial markets, sources and application of investment funds for these markets, and the future structure of market and trading mechanisms. The NASD[®] also participated in a meeting of the International Council of Securities Association (ICSA) in France. The

ICSA meeting addressed several regulation issues, including cross-border recognition of personnel engaged in transactions, standards for proprietary trading systems, and the development of international capital adequacy standards.

Domestically, the debate over the current and future structure of markets is growing and will probably continue up to and after release of the Securities and Exchange Commission's (SEC) Market 2000 study, scheduled for publication later this year. The NASD recently appeared along with the New York and American Stock Exchanges before a hearing of the Subcommittee on Telecommunications and Finance of the Committee on Energy and Commerce of the House of Representatives. The purpose of that hearing was to review the progress that has been made in meeting the objectives of the 1975 Securities Reform Act and to explore trends in trading and technology that are most likely to determine the future structure of the U.S. securities markets.

Events like these hearings and efforts like the Market 2000 study point up the need for the NASD to continue addressing a number of quality-of-market issues. These include customer limit-order protection in The Nasdaq Stock Market,SM the adoption of a "short-sale rule" for Nasdaq, issues related to the payment-for-order-flow controversy, and the operation and accessibility of the Small Order Execution System (SOES) and SelectNet.

• **Market Services** — Concerned that companies with major stockholders or control persons under SEC or self-regulatory organization sanctions might seek listing on Nasdaq, the Board approved for filing with the SEC a provision to

Schedule D of the By-Laws that would give the NASD specific authority to prevent such companies from trading on Nasdaq. Right now, the NASD may apply more stringent initial or maintenance criteria only to particular securities or suspend or delist an otherwise qualified security.

The proposal would specifically authorize the NASD to deny initial listing to an otherwise qualified security if any officer, director, controlling shareholder, or other person in a position to influence management decisions has been:

— Barred or suspended from participating in the securities industry by the SEC or any self-regulatory organization;

— Permanently enjoined by order, judgment, or decree of any court of competent jurisdiction from participating in the securities industry, or from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security; or,

— Convicted of any felony involving the purchase or sale of any security arising out of such person's participation in the securities or commodities industry.

• **Regulation** — The Board approved for filing with the SEC an amendment to Appendix F of the Rules of Fair Practice that would raise the limit on non-cash sales incentive compensation paid by a sponsor or affiliate of a sponsor of a public direct participation program to each associated person of a member during any year from \$50 to \$100. Such non-cash sales incentive compensation typically involves small souvenir-type items provided by program sponsors to associated persons of a member after execution of a selling agree-

ment with them.

The Board approved publication of a *Notice to Members* soliciting member comments on changes to the Board's Free-Riding and Withholding Interpretation and another to provide guidance on the application of the Interpretation. These proposals to update the Interpretation would affect a variety of areas, including securities to be covered by the interpretation; the interpretation's applicability to secondary offerings; definition of immediate family; its applicability to persons with limited registration or limited purpose broker/dealers; and treatment of investment partnerships and venture capital investors.

• **Member Services** — Proposed changes to the Arbitration Code, approved by the Board, will establish an Offer-of-Award pilot program for cases where the amount in controversy was \$250,000 or more. The pilot will run for two years from the date of SEC approval. The purpose of this Offer-of-Award proposal is to encourage all parties to an arbitration to evaluate and resolve cases in a timely and reasonable fashion. Basically, the measure permits any party to an arbitration to make an offer of award 60 days after filing an answer or more than 15 days before the arbitration hearing begins. If accepted, the parties to the offer must settle it within 30 days. If the offer is not accepted and the case concludes with a lower award than the last offer the party did not accept, that party would have to pay the reasonable costs (including expert witness fees) and reasonable attorneys' fees that the offering party incurred subsequent to the offer of award. The arbitration panel would determine the amount of the additional payment.

The Board approved resolutions relating to the creation of a captive insurance subsidiary for purposes of reinsuring the NASD's fidelity bonding program. Such a subsidiary would, in the Board's view, provide the NASD with the opportunity to control more effectively the standards of coverage and to capture the profits of the program for the benefit of the NASD member firm/policyholders. The Board resolutions approved organizing and funding the subsidiary.

Following review of member gross income reports, the Board has proposed a credit adjustment to member assessments to reflect more closely the assessment revenue budgeted for 1993. If the SEC approves, the amount of the credit set forth in Section 1(d) of Schedule A to the By-Laws would increase to 62 percent from 59 percent and would apply to the entire calendar year 1993.

The NASD has filed with the SEC an amendment to Section 2 of Schedule A related to mass transfers of registrations. If approved, the change would provide a discount for members filing applications to re-register or transfer the registration of associated persons when acquiring all or part of another member's business. The proposal will discount the current fee by 10 percent for 1,000 to 1,999 applications; 20 percent for 2,000 to 2,999 applications; 30 percent for 3,000 to 3,999 applications; 40 percent for 4,000 to 4,999 applications; and 50 percent for 5,000 or more applications.

• **Advisory Council Recommendations** — The Advisory Council, composed of chairmen of the District Business Conduct Committees and the Market Surveillance Committee, recently met and provided the Board with

the following items for it to consider:

— Supported NASD efforts to formulate a position on stock accumulation in advance of research reports for The Nasdaq Stock Market and the over-the-counter markets as well as the applicability of any such position to various OTC equity and debt instruments.

— Recommended an NASD review of security currently in place at its District offices and Executive office with a view to improving it where needed.

— Supported increased training and education of District Committee members to include sessions for members at the annual NASD-sponsored securities conferences as well as the development of additional training at the District and Market Surveillance Department level.

— Encouraged the NASD to expand the attorney adviser program that provides business hearing conduct panels with assistance in addressing procedural issues, providing legal guidance, and interpreting securities rules and regulations.

— Recommended the development of audio-visual educational materi-

als dealing with rule requirements for members to use in their internal compliance and supervisory programs.

— Recommended that the NASD remind members through a *Notice to Members* that Article III, Section 4 of the Rules of Fair Practice applies to commissions charged on agency transactions, including the “5% Guideline.”

— Stressed the need to clarify the applicability of Article III, Section 40 of the Rules of Fair Practice to the activities of registered representatives who also function as investment advisers.

NASD DISCIPLINARY ACTIONS

Disciplinary Actions Reported for June

The NASD® is taking disciplinary actions against the following firms and individuals for violations of the NASD Rules of Fair Practice; securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board. Unless otherwise indicated, suspensions will begin with the opening of business on Monday, June 21, 1993. The information relating to matters contained in this Notice is current as of the fifth of this month. Information received subsequent to the fifth is not reflected in this publication.

Firms Expelled, Individuals Sanctioned

Trend Securities, Inc. (San Antonio, Texas), Thurman Earl Bachman (Registered Principal, San Antonio, Texas), Lloyd C. Gage (Registered Representative, San Antonio, Texas), Steve Jay Kitchen (Registered Principal, San Antonio, Texas), and Gary Dean Cadena (Associated Person, San Antonio, Texas). The firm was fined \$10,000, expelled from NASD membership, and required to disgorge \$48,462. Bachman and Gage were each suspended from association with any NASD member in any capacity for five years.

Kitchen and Cadena submitted an Offer of Settlement pursuant to which they were suspended from association with any NASD member in any capacity for five years. Without admitting or denying the allegations, Kitchen and Cadena consented to the described sanctions and to the entry of findings that the firm, acting through Bachman, Gage, Kitchen and Cadena, permitted persons associated with the firm to sell units of non-exempt securities when such persons were not qualified or registered with the NASD as representatives.

Firms Fined, Individuals Sanctioned

Cambridge-Newport Company, Inc. (Springfield, Massachusetts) and Eric J. Youngquist (Registered Principal, Windsor, Connecticut) submitted a Letter of Acceptance, Waiver and Consent pursuant to which they were each fined \$20,000. In addition, the firm was prohibited from self clearing mutual fund wire-order transactions and Youngquist was barred from association with any NASD member in any managerial, supervisory, or principal capacity.

Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Youngquist, engaged in a securities business while failing to maintain its required minimum net capital. The NASD also found that the firm, acting through Youngquist, failed to prepare and maintain its books and records and filed false and misleading FOCUS reports with the NASD. In addition, the NASD determined that the firm, acting through Youngquist, failed to comply with Securities and Exchange Commission (SEC) Rule 15c3-3 by improperly withdrawing funds from the firm's Special Reserve Account for the Exclusive Benefit of Customers and depositing the funds into other accounts of the firm and its parent company.

Firms and Individuals Fined

VSR Financial Services, Inc. (Leawood, Kansas) and Donald J. Beary (Registered Principal, Overland Park, Kansas) submitted an Offer of Settlement pursuant to which they were fined \$14,955, jointly and severally. Without admitting or denying the allega-

tions, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Beary, failed to record transactions on its books and records or to maintain copies of any documents relating to the transactions in its files. In addition, the NASD found that the firm, acting through Beary, failed to properly supervise another individual.

Individuals Barred or Suspended

Charles A. Arrington, Jr. (Registered Representative, Alsip, Illinois) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Arrington consented to the described sanctions and to the entry of findings that he signed two public customers' names to disbursement request forms without their knowledge or consent and used the funds totaling \$1,273.65 to pay premiums on unrelated customers' life insurance policies.

John R. Banks (Registered Representative, Warren, Ohio) was fined \$15,000, barred from association with any NASD member in any capacity, and required to pay \$485 in restitution to insurance customers. The sanctions were based on findings that Banks misappropriated insurance customer funds totaling \$485 intended for payment of monthly premiums. In addition, Banks failed to respond to NASD requests for information.

Dwight Hastings Barlow (Registered Representative, Staten Island, New York) was fined \$75,000 and barred from association with any NASD member in any capacity. The fine may be reduced by any amount of resti-

tution that Barlow pays to a public customer. The sanctions were based on findings that Barlow executed transactions in the account of a public customer without the prior authorization, knowledge, or consent of the customer. To facilitate this activity, Barlow caused the address of the same customer to be changed so that her confirmations were mailed directly to his home address.

Nancy Lee Brandstatter (Registered Representative, Los Altos Hills, California) was fined \$120,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Brandstatter misappropriated \$137,096.15 belonging to 10 public customers and converted the funds to her own use and benefit. Brandstatter also failed to respond to NASD requests for information.

James Eldridge Cartwright (Registered Principal, West Hempstead, New York) was fined \$20,000, barred from association with any NASD member as a general securities principal, and required to requalify by examination in any capacity that he chooses to function.

The sanctions were based on findings that a former member firm, acting through Cartwright, failed to employ a registered financial and operations principal as required by a previous disciplinary action. The firm, acting through Cartwright, also effected securities transactions without maintaining its required minimum net capital and failed to disclose certain loans on its general ledger.

In a separate action, Cartwright was fined \$20,000, required to demonstrate payment of an arbitration award, and barred from association

with any NASD member in any capacity. The National Business Conduct Committee (NBCC) imposed the sanctions in the latter case for Cartwright's failure to pay an arbitration award.

Kenneth E. Cooner (Registered Principal, Destin, Florida) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$5,000 and suspended from association with any NASD member in any principal capacity for two weeks. Without admitting or denying the allegations, Cooner consented to the described sanctions and to the entry of findings that he failed to establish, maintain, and enforce proper supervisory procedures governing access of unauthorized personnel to the cashiering area at a branch office of his member firm.

Philip Jay Cooper (Registered Representative, Bronx, New York) was fined \$30,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Cooper failed to pay a \$7,360 NASD arbitration award plus a \$200 filing fee. In addition, Cooper failed to respond to NASD requests for information.

Jeffrey Dale Givens (Registered Representative, West Des Moines, Iowa) was fined \$20,000 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 4 District Business Conduct Committee (DBCC) decision. The sanctions were based on findings that Givens failed to respond to NASD requests for information concerning his termination from a member firm.

William Corley Hagan (Registered Representative, Des

Plaines, Illinois) was fined \$75,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Hagan participated in private securities transactions without notifying his member firm that he intended to engage in such activities. Hagan also failed to respond to NASD requests for information.

Thomas G. Kibler (Registered Representative, Circle Pines, Minnesota) was fined \$15,000, suspended from association with any NASD member in any capacity for 30 days, and required to requalify by examination as a registered representative. The SEC affirmed the sanctions following an appeal of a June 1992 NBCC decision. The sanctions were based on findings that Kibler executed transactions involving a common stock in the accounts of three public customers without their authorization.

Barry A. Loomis (Registered Representative, Ottawa, Illinois) was fined \$114,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Loomis received from insurance customers \$17,502.62 intended for the purchase of insurance. Loomis failed to follow the customers' instructions and, instead, used the funds for other purposes. Loomis also failed to respond to NASD requests for information.

Allison A. Magee (Registered Representative, Scottsdale, Arizona) was fined \$100,000, barred from association with any NASD member in any capacity, and required to pay \$13,350 in restitution to a public customer or to any other person or entity which has since recompensated the customer.

The sanctions were based on findings that Magee obtained 12 checks

totaling \$13,350 payable to a public customer, caused the payee's endorsement to be forged on the checks, and converted the funds to her own use and benefit. In addition, Magee changed the same customer's address on account records to an address where she received mail without the customer's knowledge or authorization. Magee also failed to respond to NASD requests for information.

Jack M. Mardack (Registered Representative, Jackson Heights, New York) was fined \$50,000 and barred from association with any NASD member in any capacity. The fine may be reduced by any amount of restitution paid to customers or his member firm. The sanctions were based on findings that Mardack executed transactions in the accounts of public customers without the prior knowledge, authorization, or consent of the customers. In addition, Mardack failed to respond to NASD requests for information.

Michael H. Novick (Registered Principal, Boulder, Colorado) was fined \$52,754.27 and barred from association with any NASD member in any capacity. The NBCC imposed the sanctions following an appeal of a District 8 DBCC decision. The sanctions were based on findings that a former member firm, acting through Novick, effected principal sales of common stocks to public customers at unfair and unreasonable prices. The markups on these transactions ranged from 6 to 97.2 percent over the prevailing market price.

Novick has appealed this action to the SEC, and the sanctions, other than the bar, are not in effect pending consideration of the appeal.

James Allen Piersma (Registered Representative, Holland,

Michigan) was fined \$70,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Piersma engaged in private securities transactions without notifying his member firm in writing that he intended to engage in such activities. In addition, Piersma failed to respond to NASD requests for information.

Jack W. Pruitte (Registered Representative, Clarksville, Tennessee) submitted a Letter of Acceptance, Waiver and Consent pursuant to which he was fined \$10,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Pruitte consented to the described sanctions and to the entry of findings that, in an attempt to mislead a public customer into believing that a transaction was effected in his account, Pruitte altered a copy of another customer's confirmation that reflected a sell transaction. Specifically, the findings stated that Pruitte changed the customer's name on the confirmation and sent it to the first customer.

Toney L. Reed (Registered Principal, Irving, Texas) was fined \$25,000, suspended from association with any NASD member as a principal for one year, and required to requalify by examination as a principal. In addition, Reed is required to pay \$40,175 in restitution to public customers. The NBCC imposed the sanctions following an appeal of a District 6 DBCC decision. The sanctions were based on findings that a former member firm, acting through Reed, failed to comply with the NASD's Mark-Up Policy in that it effected corporate securities transactions as principal with retail customers at prices that were not fair and reasonable.

In addition, the firm, acting through Reed, allowed eight individuals to function as representatives of the firm before the effective date of their registration with the NASD, and understated the assessable income on its 1989 Assessment Report. The firm, acting through Reed, also failed to comply with the NASD's Rules of Fair Practice relating to supervision in that a principal had not approved in writing certain correspondence and transactions in private direct participation programs. Furthermore, the firm, acting through Reed, failed to maintain inventory account statements, a principal trade blotter, and principal transaction order tickets.

The firm, acting through Reed, failed to fully perform due diligence in two direct participation programs sold by the firm. Also, the firm, acting through Reed, maintained principal registrations for 12 individuals who were not acting in a principal capacity, and permitted another individual to engage in the securities business of the firm and to receive commissions without being registered in any states.

Reed appealed this action to the SEC, and the sanctions are not in effect pending consideration of the appeal.

Marc Barry Resnick (Registered Representative, Bell Canyon, California) was fined \$20,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Resnick failed to respond to NASD requests for information concerning his termination from a member firm.

Damon Stephan Ridley (Registered Representative, Indianapolis, Indiana) was fined \$20,000 and barred from association with any NASD member in

any capacity. The sanctions were based on findings that Ridley failed to respond to NASD requests for information concerning his termination from a member firm.

Albert F. Smith (Registered Representative, Buffalo, New York) was fined \$20,000, barred from association with any NASD member in any capacity, and required to pay \$633.30 in restitution to his member firm. The sanctions were based on findings that Smith misappropriated insurance customer funds totaling \$633.30 that were designated for insurance premium payments. In addition, Smith failed to respond to NASD requests for information.

Gary Clifford Smith (Registered Principal, Carthage, North Carolina) was fined \$5,000, barred from association with any NASD member in any capacity except Series 6 registration, and required to function only under daily one-to-one supervision. The NBCC imposed the sanctions following an appeal of a District 7 DBCC decision. The sanctions were based on findings that Smith failed to pay a \$71,274.22 arbitration award and \$3,750 in forum fees.

Timoteo Torres (Registered Representative, Long Beach, California) was fined \$10,000 and barred from association with any NASD member in any capacity. The fine may be reduced by a payment to his member firm not to exceed \$700.

The sanctions were based on findings that, without an insurance customer's knowledge or consent, and through the use of forged documents, Torres caused a loan to be issued by his member firm on a life insurance policy issued to a public customer. Torres used the proceeds of such loan to purchase a new

policy for the customer, however, since the premium was not paid on the policy, it lapsed. Torres then transmitted a request for the withdrawal of accumulated dividends from the customer's original life insurance policy and submitted an application for reinstatement of the new policy, without the customer's knowledge or consent. As a result of this activity, Torres received \$698.75 in commissions.

Gordon Scott Venters (Registered Representative, Orlando, Florida) was fined \$2,500, suspended from association with any NASD member in any capacity for one day, and required to requalify by examination as a registered representative. The SEC affirmed the sanctions following an appeal of a February 1992 NBCC decision. The sanctions were based on findings that Venters recommended and caused shares of a common stock to be purchased in the account of a public customer without having reasonable grounds for believing such recommendations were suitable for the customer.

Raymond O. Wagoner (Registered Representative, Indianapolis, Indiana) was fined \$176,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Wagoner received from 42 insurance customers \$81,154.67 with instructions to use such funds to pay for insurance policies. Wagoner failed to follow the customers' instructions and applied only \$39,078.27 as instructed, and used the remaining \$42,076.40 for purposes other than to benefit the customers.

In addition, Wagoner received from a public customer \$14,448.39 with instructions to purchase mutual funds. Wagoner failed to follow the customer's instructions and used

the funds for purposes other than to benefit the customer. Wagoner also failed to respond to NASD requests for information.

Lenora Warren (Registered Representative, Baton Rouge, Louisiana) submitted a Letter of Acceptance, Waiver and Consent pursuant to which she was fined \$50,000 and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Warren consented to the described sanctions and to the entry of findings that she accepted two \$5,000 cashiers' checks from a public customer, endorsed and deposited the checks into her personal account, thereby converting the funds to her own use without the customer's knowledge or consent.

Alexander J. Wu (Registered Representative, New York, New York) was fined \$50,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that, without obtaining necessary permission to do so, Wu removed from his branch manager's file cabinet prospecting leads that were owned by other brokers at the branch office. In addition, Wu failed to respond to NASD requests for information.

Individual Barred for Failure to Comply With Sanctions

Paul M. Michalovsky, New York, New York

Firms Suspended

The following firms were suspended from membership in the NASD for failure to comply with formal written requests to submit financial information to the NASD. The

actions were based on the provisions of Article IV, Section 5 of the NASD Rules of Fair Practice and Article VII, Section 2 of the NASD By-Laws. The date the suspension commenced is listed after each entry. If the firm has complied with the requests for information, the listing also includes the date the suspension concluded.

Van H. Alford Securities, Inc., Baton Rouge, Louisiana (April 22, 1993)

America/Southwestern Securities Group, Inc., Fort Worth, Texas (April 22, 1993)

The Bostonian Group Securities Corp., Chestnut Hill, Massachusetts (April 22, 1993)

Bucchieri Asset Management, Inc., Denver, Colorado (May 14, 1993)

Cashco Capital Corporation, Chicago, Illinois (April 22, 1993 to May 11, 1993)

Collaborative Equities, Inc., Boston, Massachusetts (April 22, 1993)

Deerpath Securities Co., Inc., Lake Forest, Illinois (April 22, 1993)

Fairfax Securities Corporation, Alexandria, Virginia (May 14, 1993)

Fundamental Brokers, New York, New York (April 26, 1993)

Holford Securities (U.S.), Inc., Irvine, California (April 22, 1993)

IICC-Tradeco, Inc., New York, New York (May 14, 1993)

KAJ Financial Corp., Los Angeles, California (April 22,

1993)

Lewis Sims & Letterman, Inc., Kansas City, Missouri (April 22, 1993)

Mutual Fund Execution Services, Inc., Washington Crossing, Pennsylvania (April 22, 1993)

Plexus Group, Inc., Santa Monica, California (April 22, 1993)

Pope Investments, Brandon, Mississippi (April 22, 1993)

John F. Ramsey Investments Securities, Oakland, California (April 22, 1993)

SST Investor Services, Inc., Costa Mesa, California (April 22, 1993 to May 19, 1993)

Sanborn Capital Management, Larkspur, California (April 22, 1993)

Southwest Merchant Group, Inc., Dallas, Texas (April 22, 1993 to April 30, 1993)

R.J. Telese & Company, Sarasota, Florida (May 19, 1993)

Varel, John G., Haleiwa, Hawaii (April 22, 1993)

Walston Securities, Inc., New York, New York (April 22, 1993)

West-Rim Securities, Inc., Los Angeles, California (May 19, 1993)

Winthrop Investments, Indianapolis, Indiana (April 22, 1993)

NASD Announces Disciplinary Action Against Prudential Securities Incorporated

The NASD has taken disciplinary action against Prudential Securities Incorporated (Prudential) for certain activities in the firm's Little Rock, Arkansas and Memphis, Tennessee branch offices.

Pursuant to a Letter of Acceptance, Waiver, and Consent, in which the firm neither admitted nor denied the allegations, Prudential was censured and has paid a \$250,000 fine. In addition, Prudential agreed to institute training programs in its Little Rock and Memphis branch offices.

NASD found that Prudential's failure to supervise properly the activities of certain employees in the Little Rock office resulted in an unsuitable level of trading in the account of an institutional public customer, and an eventual settlement by the firm in the amount of \$700,000. In addition, the firm's failure to supervise properly the maintenance and preparation of its books and records in the Little Rock office resulted in certain employees improperly receiving commissions through the production numbers of other registered representatives, and compensation being paid to employees by check or other means not reflected on the firm's books and records.

The NASD also determined that Prudential failed to supervise properly the activities of a firm employee in its Memphis office who was found to have conducted an unsuitable level of trading in an institutional customer's account.

The NASD found that Prudential violated the NASD's Rules of Fair Practice. Other individuals that were involved in this matter are

currently the subject of separate disciplinary actions.

This disciplinary action was taken by the District 5 DBCC in New Orleans, Louisiana, which maintains jurisdiction over members with main and branch offices in Louisiana, Mississippi, Alabama, Arkansas, Tennessee, Oklahoma, and Kentucky.

SEC Affirms NASD Actions Against Officer, Salesman

The NASD announced SEC affirmation of an NASD disciplinary action.

The SEC largely affirmed findings and sanctions entered by the NASD in a 1988 decision against Randolph K. Pace of New York, New York and Thomas Henry of Oklahoma City, Oklahoma. Pace was co-chief executive officer of Rooney, Pace, Inc., a former member firm located in New York City which was previously expelled by the NASD. Pace also oversaw the firm's over-the-counter trading department. Henry was a salesman in Rooney, Pace's Oklahoma City branch office.

The NASD found that Pace participated in a manipulation of American Educational Computer, Inc., (AEC), thereby violating the NASD's rules which prohibit members and associated persons from engaging in securities transactions through the use of manipulative, deceptive, and other fraudulent devices or contrivances. The NASD also found that Pace failed to supervise adequately the firm's salesmen to prevent them from defrauding Rooney, Pace's customers and engaging in unauthorized trading in AEC stock. Pace was fined \$100,000, suspended from association with any NASD member in

any capacity for two years, and prohibited from working in a supervisory capacity with any NASD member for an additional five years. The NASD found that Henry knowingly acted in furtherance of the manipulation. He was fined \$10,000 and suspended from association with any NASD member in any capacity for one year.

The SEC found "overwhelming evidence" to support the NASD finding that Rooney, Pace manipulated the price of AEC. Among other things, Rooney, Pace dominated and controlled the market in AEC; consistently led the market at the close; increased its high bid at a time when the firm already had a substantial inventory position in the stock; supported an inflated price for the stock at a time when the company's financial performance was steadily deteriorating; effected retail sales below its inside bid; made misrepresentations to customers; and effected high volume unauthorized trading in one customer account. The SEC found that the "effect of the scheme was to suspend the normal interplay of market forces, and to cause a misleading appearance that there was sufficient market interest in the security to sustain a price that was, in fact, not an accurate reflection of the security's worth." When Rooney, Pace ceased supporting the price of AEC, the stock immediately tumbled from \$9 to \$4.50, another indication that Rooney, Pace had manipulated the market.

The SEC rejected Pace's claim that he was unaware of the manipulation. The SEC found "much circumstantial support" for the NASD conclusion that Pace knew about the manipulation at the scheme's very apex, and set up an undisclosed inventory account to profit from the manipulation by unloading the firm's inventory at

prices Pace knew to be artificially inflated. In so doing, the SEC found that Pace “put benefit to his firm above integrity of the market and the interest of his customers” Almost all of the shares sold from this account ended up with one Oklahoma City customer who did not authorize the purchases. The SEC stated that even a rudimentary inquiry by Pace into the account would have revealed the illicit activity that was occurring. However, Pace examined the account only to determine whether there was sufficient buying power to support the purchases. The SEC concluded that Pace “knowingly breached a fiduciary obligation” to this customer. According to the SEC, the NASD sanctions against Pace were fully warranted because of the “egregiousness of his conduct” in participating in a manipulative scheme and his “grossly deficient” supervision.

The SEC affirmed NASD findings that Henry assisted in the manipulation by misrepresenting AEC’s future prospects to induce sales or persuade customers not to sell the security; giving a guarantee against loss to a customer to prevent him from selling the security; failing to disclose to customers material adverse information regarding the character of the market in AEC; accepting customer sales orders without intending to execute them and “lying outright” to at least one of those customers that sales had in fact occurred.

NASD Expels Firm, Fines Traders in GNMA Scam

The NASD took disciplinary action against Steven Kochensparger of Upper Arlington, Ohio, fining him \$200,000, requiring him to make restitution to a customer, and barring him from association with any

member in any capacity. In addition, Roger Parsons of Baltimore, Ohio was fined \$165,000 and barred from association with any member in any capacity; Orion Securities, Inc., of Englewood, Colorado was expelled from membership in the Association; and Douglas W. Nutt of Greenwood Village, Colorado, the President of Orion, was barred from associating with any member in any capacity. In addition, Nutt and Orion were fined \$400,000, jointly and separately.

This matter primarily related to misrepresentations, omissions, and related misconduct concerning bonds issued by the Government National Mortgage Association (GNMA) which were purportedly being held at Columbus Equities International, Inc., then known as Parsons Securities, Inc., a former member located in Columbus, Ohio. The NASD found that in seven separate transactions in 1989 and 1990, Steven Kochensparger, a registered representative with Parsons Securities, fraudulently represented to lenders, insurers, and other institutions that Parsons Securities was holding certain GNMA bonds that were available for collateral to secure loans or to enhance the balance sheet of insurance companies so they could continue conducting business. The GNMA bonds were clearly not on deposit as represented by Kochensparger, and Kochensparger had no basis to confirm, as he did, that the borrower or a third party owned the bonds; that the bonds were free and clear of all liens and encumbrances; or that if the value of the bonds declined, Kochensparger would liquidate the bonds or transfer them to the lender. As a result of Kochensparger’s misconduct, lenders lost several million dollars. One of the lenders, a California savings and loan insti-

tution, went into receivership.

Parsons, who was the President of Parsons Securities, was charged with failing to properly supervise Kochensparger. Without admitting or denying the allegations, Parsons settled this and several other pending actions relating to alleged net capital, markup, and SEC cold-call rule violations. As to the GNMA matter, the NASD found, among other things, that Parsons received numerous telephone inquiries concerning Kochensparger’s activities, but took no action, and that his failure to investigate Kochensparger’s conduct allowed the fraudulent scheme to continue.

The involvement of Nutt and Orion stems from a scheme involving a \$500,000 loan obtained by one of their investment banking clients from a Minnesota commercial lender. The principal collateral for the loan was supposed to be a GNMA bond purportedly being held by Parsons Securities which had been pledged by another of Orion’s clients, Dublin Osaka Group, Inc. Several months before this loan was obtained, Nutt, under mysterious circumstances, bought 372,000 shares of Dublin Osaka, which was approximately one-third of the company’s purported free-trading stock, from three shareholders at an average price of \$.0006 per share. Orion then entered quotes in the NBQ Pink Sheets at \$5 bid, \$5.25 ask, effected several trades at these prices, while subsequently trading the stock at prices of \$1.25 to \$1.75 per share, thereby realizing a profit of almost \$400,000. The NASD found that Nutt and Orion did not satisfy their burden of demonstrating that this stock was exempt from registration and freely tradable. The NASD also found that Nutt and Orion effected fraudulent markdowns when initially purchasing these shares, and

alternatively concluded that the receipt of stock was illicit consideration for becoming a market maker.

Although Nutt and Orion have appealed to the SEC, the bar and expulsion were not stayed by the SEC pending appeal. In denying their request for a stay, the SEC found that Nutt and Orion had not demonstrated a substantial possibility of prevailing on the merits of their appeal.

The NASD acknowledges the assistance of the Oklahoma Department of Securities in the AEC matter. "Both of these investigations were carried out by the NASD's Anti-Fraud Department in Washington, D.C., and demonstrates the varied scope of the NASD's overall efforts to prevent manipulative activity and abusive sales practices in the securities industry," says John E. Pinto, Executive Vice President, Regulation. "It also reflects the very positive results that can be achieved by working on a coordinated basis with state regulators throughout the country."

NASD Announces Disciplinary Action Against Partnership Exchange Securities Corporation And Two Individuals

The NASD has taken a disciplinary action against Partnership Exchange Securities Company (PESCO) of Oakland, California, Ronald Thomas Baker of Walnut Creek, California, and James Frank Fotenos of San Francisco, California.

PESCO, Baker, and Fotenos were censured and fined a total of \$90,540.29 and ordered to make restitution to customers in the amount of \$89,176.30. The fine is to be reduced by the amount of the restitution demonstrated as paid to

customers. The disciplinary action was initiated by the District DBCC 1 in San Francisco and the NASD's decision was issued by its NBCC following an appeal.

The NBCC found that PESCO, acting through Baker and Fotenos, charged unfair markups in the purchase and sale of limited partnership interests in the secondary market. Specifically, the NBCC found that during 1989 the respondents charged unfair markups to customers in 36 transactions. The markups ranged from 15.94 percent to 359.46 percent based on PESCO's cost of the securities.

The markups as computed included a transfer fee generally in the amount of \$250 charged by PESCO to each seller. This fee was separately disclosed to the sellers on PESCO's confirmations. This fee was retained by PESCO. The NASD considered the transfer fee to be part of the unfair markups, and ordered it returned to sellers as part of the order of restitution.

In issuing its decision, the NASD specifically rejected the respondents' contention that the ultimate purchasers and sellers involved were not PESCO's customers. PESCO had argued that because the sellers and purchasers were represented by third parties, including brokers, it had no fiduciary obligations to them, and could, therefore, buy and sell at whatever prices it could negotiate. The NASD noted that the role of these third-party brokers was limited strictly to finding a buyer or seller for their clients and negotiating a price; from that point on, the clients dealt directly with PESCO. PESCO did not buy or sell securities with these or other broker/dealers in an inter-dealer market. The NASD found that the third-party brokers took no part in effecting the transaction, title trans-

fer, or guarantee distribution. PESCO bought directly from sellers and sold directly to buyers. PESCO executed the assignments and handled the paperwork, and was responsible for transferring title and paying distributions during the process. The individual buyers paid PESCO which then paid commissions to the third-party brokers, and paid the sellers. Any commissions owed by sellers were also remitted to PESCO which, in turn, wrote and sent commission checks to third-party brokers.

The NASD further rejected the respondents' contention that the NASD had improperly calculated markups based on PESCO's cost in transactions which were not contemporaneous with retail sales. The Complaint alleged that the securities had been purchased from the sellers by PESCO and held by PESCO for periods ranging for as many as 56 calendar days. Under the specific facts and circumstances in this case, the NBCC found no evidence of an active, competitive inter-dealer market and concluded that it was not possible to ascertain any "current market price" on the basis of inter-dealer sales. In that regard, the NASD noted that applying a contemporaneous cost standard to the secondary market for limited partnership interests would be illogical because it would assume certain similarities between the markets for equity and debt securities and the limited partnership secondary market that did not exist in this particular case. In making this finding, the NBCC considered that none of PESCO's purchases was effected on any organized market, the securities did not trade on any market or exchange, most trades were conducted on an agency basis, and quotations were subject to negotiation. Based on this analysis, the NASD also concluded that it would reject PESCO's

contention that the firm was entitled to the difference between the purchase and sale price because it was at risk. The NASD stated that even a firm that puts its capital at risk to make a market is only entitled to be compensated for that risk by taking the spread in an active, competitive market, which did not exist here.

The NBCC further found that any markup in excess of 8 percent was

unfair in the PESCO case. Elaborating further, the NBCC said, “we find that an 8 percent markup is fair under the particular facts and circumstances of this case, but [emphasize] that *this decision should not serve as a license to other member firms to charge 8 percent, since each case must be considered on its own merits.*” In that regard, the NBCC reiterated the applicability of its long-stand-

ing 5 percent markup policy to secondary trading in direct participation programs, expressly stating that “. . . the NASD’s Mark-Up Policy should be applied to the sale of Direct Participation Program units in the secondary market.”

The respondents have appealed the decision to the SEC.

FOR YOUR INFORMATION

Pennsylvania Increases Agent Registration, Re-registration, and Renewal Fees

On May 4, 1993, Pennsylvania increased its agent registration and re-registration fees to \$75 to be effective on CRD as of May 7, 1993. Agent renewal fees increased to \$60. Firm registration and renewal fees will remain at \$250. If you have any questions regarding these changes, please call the NASD's Member Services Phone Center at (301) 590-6500.

NASD Member Voting Results

As a member service, the NASD publishes the result of member votes on issues presented to them for approval in the monthly *Notices to Members*. Most recently, members voted on the following issue:

- ***Notice to Members 93-15*** — Proposed Amendments to Articles VII and XII of the By-Laws and Article III of the Rules of Fair Practice to Make All Rule Approval Procedures Under the NASD's By-Laws Uniform. Ballots For: 1,683; Against: 478; and Unsigned: 11.

Questions regarding this item should be directed to Stephen Hickman, President's Office, at (202) 728-8381.

SPECIAL NASD NOTICE TO MEMBERS 93-40

Request for Comments on Proposed Amendments to the Free-Riding and Withholding Interpretation Under Article III, Section 1 of the Rules of Fair Practice

Suggested Routing

- Senior Management
- Corporate Finance
- Government Securities
- Institutional
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training

Executive Summary

The NASD requests comment on proposed amendments to the Free-Riding and Withholding Interpretation under Article III, Section 1 of the Rules of Fair Practice. These amendments would change a number of the Interpretation's provisions. The complete text of the Interpretation follows this Notice.

Background

At its May 1992 meeting, the NASD Board of Governors (Board) appointed a special committee to examine the Free-Riding and Withholding Interpretation (Free-Riding Committee) to determine if the Interpretation's restrictions, definitions and obligations are relevant in today's securities markets. The Committee was comprised of representatives of the NASD's National Business Conduct, Corporate Financing, and Insurance Affiliated Members Committees as well as the members of the Board. The Board also asked the Committee to examine various interpretative issues that had been raised with the NASD. The Free-Riding Committee met numerous times from May 1992 until April 1993 and received input and suggestions, both in writing and in person, from members, issuers, law firms, the NASD Legal Advisory Board, and the staff of various NASD departments.

Overview of Free-Riding and Withholding Interpretation

The purpose of the Interpretation is to protect the integrity of the public offering system by ensuring that members make a bona fide public distribution of "hot issue" securities and neither withhold such securities

for their own benefit nor use the securities to reward other persons in a position to direct future business to the member. As defined by the Interpretation, hot issues are securities of a public offering that trade at a premium in the secondary market when such trading commences. The Interpretation prohibits members from retaining such securities in their own accounts and prohibits members from using sales of such securities to directors, officers, employees, and associated persons of members and other broker/dealers. It also restricts member sales of hot-issue securities to the accounts of specified categories of persons, including among others, senior officers of banks, insurance companies, registered investment companies, registered investment advisory firms, and any other persons within such organizations whose activities influence or include the buying or selling of securities. These basic prohibitions and restrictions also apply to sales by members of hot-issue securities to accounts in which any such persons may have a beneficial interest and, with limited exceptions, to members of the immediate family of those persons restricted by the Interpretation.

NASD Compliance Department Procedures

As part of its deliberations, the Committee considered redefining the term "hot issue" to provide more guidance to the membership as to those offerings which are subject to the Interpretation. Rather than taking this approach, however, the Committee asked the staff of the NASD Compliance Department to provide guidance on the internal NASD procedures regarding hot issues. The following description is intended to provide that guidance.

The NASD's Compliance

Department in Washington, D.C. has the responsibility of reviewing the after-market quotation and trading activity of all public offerings to determine whether the securities traded in the secondary market at a price which is higher than the public offering price. If the immediate bid quotations of market makers and trade reports by broker/dealers of purchases are at prices above the public offering price on the first day of trading, the offering is deemed to be a "hot issue." The determination of a hot issue is not necessarily based on the opening bid quotation or the first reported transaction; rather, the NASD's focus is on the overall market activity as the secondary market commences and continues, which includes consideration of a pattern of bid quotations and purchases at prices exceeding the public offering price.

This review by the Compliance Department is centralized to insure consistency and uniformity throughout the NASD's 14 district offices. For a security that is characterized by current quotations, real-time trade reporting and secondary market activity which develops on completion of the offering, the NASD takes a number of factors into consideration when determining whether the issue is hot. In active and competitive securities which are normally associated with issues that list on Nasdaq or an exchange, the NASD analyzes inside bid quotations in the immediate secondary market, actual initial transactions, the volume, and the amount of the premium.

While there is no formula or absolute rule that determines precisely at what point in time secondary market trading in securities that have the characteristics described above would result in an issue being deemed hot, the primary factors that are considered are fairly

basic. Was there unsatisfied public demand for the issue at the time of the offering; was there immediate demand to buy the stock when it first opened for trading in the secondary market; could the shares purchased in the public offering be sold at a profit in the immediate secondary market?

As an example, a security with a public offering price of \$10 that opens for trading on Nasdaq or on a national securities exchange at \$10, and trades at that price for several hours, and then moves up to \$11 by the close of trading would not be considered a hot issue. Nor would a similarly priced Nasdaq or exchange listed new issue that trades down initially at \$9 3/4 from its public offering price of \$10, only to move up after several hours to close at \$10 1/2. Thus, the NASD focus is on immediate secondary market bids and transaction activity.

As referenced earlier, the regulatory process described above applies to issues where current price, volume and transactional information are accessible on a real-time basis, typically (i.e., Nasdaq or exchange-listed issues). For underwritings of issues that do not have those characteristics, or that may be subject to other conditions such as being dominated and controlled by a particular dealer or group of dealers, or are very inactive or infrequently traded, other criteria may be used by the NASD in determining whether the issue is deemed hot. The NASD also reviews such offerings and subsequent secondary market activity for indications of possible violations of other NASD rules or federal securities laws.

The NASD through its Compliance Department will authorize the issuance of a Free-Riding and Withholding Questionnaire (Free-

Riding Questionnaire) for those hot issues that exceed certain preset and predetermined regulatory parameters determined by the NASD. While not all offerings that open at a premium are subject to a Free-Riding Questionnaire, any public offering that opens at a premium is considered a hot issue under the Free-Riding and Withholding Interpretation. District examiners routinely review for compliance with the Free-Riding Interpretation during field examinations for those hot issues that are not the subject of a Free-Riding Questionnaire.

Proposed Modifications for Member Comment

Securities to Be Covered

The Free-Riding Committee recommended that the Interpretation continue to apply to both equity and debt securities, but is seeking comment, including the views of the NASD Fixed Income Committee, on applying the Interpretation to "straight" debt securities. The Free-Riding Committee clearly believes that the Interpretation should continue to apply to convertible and high-yield debt securities. In addition, comments are solicited as to the Legal Advisory Board's suggestion that the NASD consider excluding, at least, "rated" debt from the Interpretation.

The Free-Riding Committee believes that closed-end mutual funds should remain covered by the Interpretation.

Stand-by Arrangements

The Free-Riding Committee concluded that securities purchased under a stand-by arrangement by a restricted account should not be subject to the Interpretation if:

- The stand-by arrangement is disclosed in the prospectus.
- The arrangement is the subject of a formal agreement.
- There is a representation from the underwriter that it was unable to find any other purchaser for the securities.
- An appropriate holding period for the securities be included. The Free-Riding Committee determined that for purposes of soliciting comment on the proposal it would apply the holding period of five months currently included in the Interpretation's provisions relating to conversion offerings. Comments are specifically solicited on the appropriate holding period for securities purchased under a standby agreement.

Cancellation of Trades as "Safeharbor"

The Free-Riding Committee believes that the Interpretation should make it clear that it is not a violation for a member to allocate a hot issue to a restricted person or account *if* the member cancels the trade and reallocates the security, at the public offering price, to a non-restricted account prior to the settlement date. The Committee understands that there may be implications of such cancellations and reallocations under Securities Exchange Act Rule 10b-6 and seeks comment on this issue.

Definition of Immediate Family

The Interpretation now restricts immediate family members of persons enumerated in paragraph 2 which covers persons associated with broker/dealers, and paragraphs 3 and 4 of the Interpretation which

relate to persons having a relationship with the offering and individuals related to banks, insurance companies, and other institutional type accounts (see page 262) from participating in hot issues. The rule defines immediate family members very broadly and includes such persons as father-, mother-, brother-, and sister-in-law. Members have expressed concern over the compliance difficulties of monitoring whether such persons are restricted or become restricted. The Interpretation also contains a provision that allows for immediate family members of persons designated in paragraph 2 and for persons designated in paragraphs 3 and 4 of the rule to purchase hot issues if they have the requisite investment history with the member making the hot-issue allocation, and the allocation meets certain other requirements.

The Committee's recommendations are:

1. The investment history exemption should be retained in spite of the fact that it is infrequently used and should be expanded to include the use of investment history at firms other than the member making the allocation. The burden of obtaining such information would remain with the firm making the sale.
2. The immediate family restrictions on persons other than those associated with broker/dealers (categories 3 and 4 referenced above) would be eliminated and the restriction would only apply to the enumerated individuals in those categories and to persons who are supported directly or indirectly to a material extent by the restricted person.
3. For persons associated with broker/dealers, the immediate family restrictions would continue to apply

to persons supported by the restricted individual and to allocations by the restricted individual's firm, but would no longer prohibit sales to non-supported family members by a broker/dealer other than that employing the restricted person where the restricted person has no ability to control the allocation of the hot issue. However, a violation would occur if it could be determined that the restricted person had a beneficial interest in the account to which an allocation was made.

Applicability to Persons With Limited Registration or Limited Purpose Broker/Dealers

The Free-Riding Committee believes that individuals with various limited purpose registrations should not be considered to be restricted persons. The categories would be persons registered as representatives or principals in registration categories limited to investment company securities, variable contracts, and Direct Participation Program securities. Comment is solicited on the propriety of exempting any securities industry professionals and, if appropriate, the proper scope of such an exclusion.

Investment Partnerships

The Interpretation, in dealing with the topic of "Investment Partnerships and Corporations," generally disallows sales to the partnership or corporation if restricted persons have a beneficial interest in the entity. In the August 1992 *Notice to Members*, the Board announced it was going to allow investment partnerships on an interim basis to use a "carve out" mechanism to prevent restricted persons in the partnerships from participating in hot-issue allocations. This carve-out mecha-

nism involves the member making such allocation to set up a separate account for these transactions and obtaining from the partnership and its accountants documentation (the partnership agreement) that indicates the restricted persons are prevented from participating in hot-issue allocation.

The Free-Riding Committee believes the carve-out methodology is the most appropriate and should apply both to investment partnerships having restricted persons as investors (as allowed by the August 1992 Notice) and to partnerships that the restricted person or entity is engaged in the manages. The Free-Riding Committee recommends substituting an independent certified public accountant's opinion for the opinion of counsel currently called for in the Interpretation as well as those described below since such opinions are more certifications of fact than a true legal opinion and obtaining such an opinion from a law firm creates undue expense.

The required mechanisms are as follows:

1. The investment partnerships will establish a separate brokerage account, with a separate identification number, for its new-issue purchases. At the end of each fiscal year, the general partners will certify in writing to their independent certified public accountants that: (a) all hot issues purchased by the partnership were placed in this new-issue account; (b) the partners participating in the new-issue account are not restricted persons under the Interpretation; and (c) no management fees are based on the performance of securities in the new-issue account.

2. Before executing the initial hot-issue transaction, the partnership's

accountants will provide a certification that complies with paragraph B of the section of the Interpretation entitled "Investment Partnerships and Corporations."

3. As part of its audit procedure for the partnership, the independent certified public accountant will confirm in writing to the partnership that all allocations for the new-issues account were made in accordance with the provisions of the applicable partnership agreement that restricts participation in hot-issue purchases.

4. The partnership will maintain in its files copies of the certifications, representations, and confirmations referred to in paragraphs (1) - (3) above for at least three years following the last purchase of a hot issue for the new-issue account.

5. The partnership will accept investment funds from other partnerships if such other partnerships provide the same documentation and assurances described in paragraphs (1) - (4) that restricted persons will not participate in the purchase of hot issues.

6. The certifications and documents required in paragraphs (1) - (3) shall be provided to the member holding such account at such time as these certifications and documents are filed with the partnership and its independent certified public accountant and the member shall make such documentation available to the NASD on request.

Foreign Mutual Funds

The Interpretation excludes from entities restricted as Investment Partnerships or Corporations, investment companies registered under the Investment Company Act of 1940. The Free-Riding

Committee believes foreign mutual funds which are subject to a similar scheme of regulation as that governing domestic funds should be similarly exempted. Comments are solicited on the proper scope of such an exemption and the appropriate methodology for determining the similarity of regulation.

Venture Capital Investors

The Committee recommends allowing purchases by a venture capital investor (either a fund or an individual) if the following conditions are met:

1. One year of preexisting ownership of the company's securities.

2. No increase in the investor's percentage ownership above that of the securities held for the prior year as a result of the purchase of the new issue.

3. A lack of special terms connection with the purchase.

4. A six-month lock-up period for the newly purchased securities.

Comment is solicited on the appropriate lock-up period.

Requests for Comments

The NASD asks members and other interested persons to comment on the proposed amendments to the Free-Riding Interpretation. Comments should be directed to Mr. Stephen D. Hickman, Corporate Secretary, National Association of Securities Dealers, Inc., 1735 K Street, NW, Washington, DC 20006-1500.

Comments must be received **no later than July 31, 1993**.
Comments received by this date

will be considered by the National Business Conduct Committee and the Board. Before becoming effective, the proposed amendment must be approved by the Board, adopted by the membership, and filed with the SEC for final approval.

Questions concerning this Notice should be directed to T. Grant Callery, Vice President and General Counsel, at (202) 728-8285, or Craig L. Landauer, Associate General Counsel, at (202) 728-8291. Questions concerning the Compliance Department procedures should be directed to P. William Hotchkiss, Director, at (202) 728-8235.

Text of Proposed Amendments to Free-Riding and Withholding Interpretation Under Article III, Section 1 of the Rules of Fair Practice

(Note: Proposed language is underlined; deleted language is in brackets.)

Interpretation of the Board of Governors

“Free-Riding and Withholding”

Introduction

The following Interpretation of Article III, Section 1 of the Association’s Rules of Fair Practice is adopted by the Board of Governors of the Association pursuant to the provisions of Article VII, Section 3(a) of the Association’s By-Laws and Article I, Section 3 of the Rules of Fair Practice.

This Interpretation is based upon the premise that members have an obligation to make a bona fide public distribution at the public offering price of securities of a public

offering which trade at a premium in the secondary market whenever such secondary market begins (a “hot issue”) regardless of whether such securities are acquired by the member as an underwriter, as a selling group member, or from a member participating in the distribution as an underwriter or a selling group member, or otherwise. The failure to make a bona fide public distribution when there is a demand for an issue can be a factor in artificially raising the price. Thus, the failure to do so, especially when the member may have information relating to the demand for the securities or other factors not generally known to the public, is inconsistent with high standards of commercial honor and just and equitable principles of trade and leads to an impairment of public confidence in the fairness of the investment banking and securities business. Such conduct is, therefore, in violation of Article III, Section 1 of the Association’s Rules of Fair Practice and this Interpretation thereof which establishes guidelines in respect to such activity.

As in the case of any other Interpretation issued by the Board of Governors of the Association, the implementation thereof is a function of the District Business Conduct Committees and the Board of Governors. Thus, the Interpretation will be applied to a given factual situation by individuals active in the investment banking and securities business who are serving on these committees or on the Board.

They will construe this Interpretation to effectuate its overall purpose to assure a public distribution of securities for which there is a public demand.

The Board of Governors has determined that it shall not be consid-

ered a violation of this Interpretation if a member which makes an allocation to a restricted person or account of an offering that trades at a premium in the secondary market, cancels the trade for such restricted person or account, prior to settlement date and reallocates such security at the public offering price to a non-restricted person or account.

Interpretation

Except as provided herein, it shall be inconsistent with high standards of commercial honor and just and equitable principles of trade and a violation of Article III, Section 1 of the Association’s Rules of Fair Practice for a member, or a person associated with a member, to fail to make a bona fide public distribution at the public offering price of securities of a public offering which trade at a premium in the secondary market whenever such secondary market begins regardless of whether such securities are acquired by the member as an underwriter, a selling group member or from a member participating in the distribution as an underwriter or selling group or otherwise. Therefore, it shall be a violation of Article III, Section 1 for a member, or a person associated with a member, to:

1. Continue to hold any of the securities so acquired in any of the member’s accounts;
2. Sell any of the securities to any officer, director, general partner, employee or agent of the member or of any other broker/dealer, or to a person associated with the member or with any other broker/dealer, or to a member of the immediate family of any such person[;], provided however, that:

(a) This prohibition shall not

apply to a person in a limited registration category as that term is defined below;

(b) The prohibition shall not apply to sales to a member of the immediate family of a person associated with a member who is not supported directly or indirectly to a material extent by such person if the sale is by a broker/dealer other than that employing the restricted person and the restricted person has no ability to control the allocation of the hot issue.

3. Sell any of the securities to a person who is a finder in respect to the public offering or to any person acting in a fiduciary capacity to the managing underwriter, including, among others, attorneys, accountants and financial consultants, or to [a member of the immediate family of any such person;] any other person who is supported directly or indirectly, to a material extent, by any person specified in this paragraph.

4. Sell any securities to any senior officer of a bank, savings and loan institution, insurance company, registered investment company, registered investment advisory firm or any other institutional type account, domestic or foreign, or to any person in the securities department of, or to any employee or any other person who may influence or whose activities directly or indirectly involve or are related to the function of buying or selling securities for any bank, savings and loan institution, insurance company, registered investment company, registered investment advisory firm, or other institutional type account, domestic or foreign, or to [a member of the immediate family of any such person;] any other person who is supported directly or indirectly, to a material extent, by any person specified in this paragraph.

5. Sell any securities to any account in which any person specified under paragraphs (1), (2), (3) or (4) hereof has a beneficial interest;

Provided, however, a member may sell part of its securities acquired as described above to:

(a) persons enumerated in paragraphs (3) or (4) hereof; and

(b) members of the immediate family of persons enumerated in paragraph (2) hereof provided that such person enumerated in paragraph (2) does not contribute directly or indirectly to the support of such member of the immediate family; and

(c) any account in which any person specified under paragraph (3) or (4) or subparagraph (b) of this paragraph has a beneficial interest;

if the member is prepared to demonstrate that the securities were sold to such persons in accordance with their normal investment practice with the member, that the aggregate of the securities so sold is insubstantial and not disproportionate in amount as compared to sales to members of the public and that the amount sold to any one of such persons is insubstantial in amount.

6. Sell any of the securities, at or above the public offering price, to any other broker/dealer; provided, however, a member may sell all or part of the securities acquired as described above to another member broker/dealer upon receipt from the latter in writing assurance that such purchase would be made to fill orders for bona fide public customers, other than those enumerated in paragraphs (1), (2), (3), (4) or (5) above, at the public offering price as an accommodation to them and without compensation for such.

7. Sell any of the securities to any domestic bank, domestic branch of a foreign bank, trust company or other conduit for an undisclosed principal unless:

(a) An affirmative inquiry is made of such bank, trust company or other conduit as to whether the ultimate purchasers would be persons enumerated in paragraphs (1) through (5) hereof and receives satisfactory assurance that the ultimate purchasers would not be such persons, and that the securities would not be sold in a manner inconsistent with the provisions of paragraph (6) hereof; otherwise, there shall be a rebuttable presumption that the ultimate purchasers were persons enumerated in paragraphs (1) through (5) hereof or that the securities were sold in a manner inconsistent with the provisions of paragraph (6) hereof;

(b) A recording is made on the order ticket, or its equivalent, or on some other supporting document, of the name of the person to whom the inquiry was made at the bank, trust company or other conduit as well as the substance of what was said by that person and what was done as a result thereof;

(c) The order ticket, or its equivalent, is initialed by a registered principal of the member; and

(d) Normal supervisory procedures of the member provide for a close follow-up and review of all transactions entered into with the referred to domestic bank, trust companies or other conduits for undisclosed principals to assure that the ultimate recipients of securities so sold are not persons enumerated in paragraphs (1) through (6) hereof.

8. Sell any of the securities to a foreign broker/dealer or bank unless:

(a) In the case of a foreign broker/dealer or bank which is participating in the distribution as an underwriter, the agreement among underwriters contains a provision which obligates the said foreign broker/dealer or bank not to sell any of the securities which it receives as a participant in the distribution to persons enumerated in paragraphs (1) through (5) above, or in a manner inconsistent with the provisions of paragraph (6) hereof; or

(b) In the case of sales to a foreign broker/dealer or bank which is not participating in the distribution as an underwriter, the selling member:

(i) makes an affirmative inquiry of such foreign broker/dealer or bank as to whether the ultimate purchasers would be persons enumerated in paragraphs (1) through (5) hereof and receives satisfactory assurance that the ultimate purchasers of the securities so purchased would not be such persons, and that the securities would not be sold in a manner inconsistent with the provisions of paragraph (6) hereof;

(ii) a recording is made on the order ticket, or its equivalent, or upon some other supporting document, of the name of the person to whom the inquiry was made at the foreign broker/dealer or bank as well as the substance of what was said by that person and what was done as a result thereof; and

(iii) the order ticket, or its equivalent, is initialed by a registered principal of the member.

The obligations imposed upon members in their dealings with foreign broker/dealers or banks by this paragraph 8(b) can be fulfilled by having this foreign broker/dealer

or bank to which sales falling within the scope of this Interpretation are made execute Form FR-1, or a reasonable facsimile thereof. This form, which gives a blanket assurance from the foreign broker/dealer or bank that no sales will be made in contravention of the provisions of this Interpretation, can be obtained at any District Office of the Association or at the Executive Office. The acceptance of an executed Form FR-1, or other written assurance, by a member must in all instances be made in good faith. Thus, if a member knows or should have known of facts which are inconsistent with the representations received, such will not operate to satisfy the obligations imposed upon him by this paragraph.

Scope and Intent of Interpretation

In addition to the obvious scope and intent of the above provisions, the intent of the Board of Governors in the following specific situations is outlined for the guidance of members.

Limited Registration Category

The term limited representative shall include persons registered solely as either investment company and variable contracts products principal or representative, direct participation program principal or representative.

Issuer Directed Securities

This Interpretation shall apply to securities which are part of a public offering notwithstanding that some or all of those securities are specifically directed by the issuer to accounts which are included within the scope of paragraphs (3) through (8) above. Therefore, if a person within the scope of those paragraphs to whom securities were

directed did not have an investment history with the member or registered representative from whom they were to be purchased, the member would not be permitted to sell him such securities. Also, the "disproportionate" and "insubstantial" tests would apply as in all other situations. Thus, the directing of a substantial number of securities to any one person would be prohibited as would the directing of securities to such accounts in amounts which would be disproportionate as compared to sales to members of the public. This Interpretation shall also apply to securities which are part of a public offering notwithstanding that some of those securities are specifically directed by the issuer on a non-underwritten basis. In such cases, the managing underwriter of the offering shall be responsible for insuring compliance with this Interpretation in respect to those securities.

Notwithstanding the above, sales of issuer directed securities may be made to restricted persons without the required investment history after receiving permission from the Board of Governors. Permission will be given only if there is a demonstration of valid business reasons for such sales (such as sales to distributors and suppliers or key employees, who are in each case incidentally restricted persons), and the member seeking permission is prepared to demonstrate that the aggregate amount of securities so sold is insubstantial and not disproportionate as compared to sales to members of the public, and that the amount sold to any one of such persons is insubstantial in amount.

Stand-By Purchasers

Securities purchased pursuant to a stand-by arrangement shall not be subject to the provisions of the

Interpretation if the following conditions are met:

1. The stand-by agreement is disclosed in the prospectus.
2. The arrangement is the subject of a formal written agreement.
3. The managing underwriter represents in writing that it was unable to find any other purchasers for the securities.
4. The securities purchased shall be restricted from sale or transfer for a period of five months.

Investment Partnerships and Corporations

A member may not sell securities of a public offering which trade at a premium in the secondary market whenever such secondary market begins (“hot issue”), to the account of any investment partnership or corporation, domestic or foreign (except companies registered under the Investment Company Act of 1940) including but not limited to, hedge funds, investment clubs, and other like accounts unless the member complies with either of the following alternatives:

(A) prior to the execution of the transaction, the member has received from the account a current list of the names and business connections of all persons having any beneficial interest in the account, and if such information discloses that any person enumerated in paragraphs (1) through (4) hereof has a beneficial interest in such account, any sale of securities to such account must be consistent with the provisions of this Interpretation,

or

(B) prior to the execution of the transaction, the member has

obtained a copy of a current opinion from [counsel admitted to practice law before the highest court of any state] the partnership’s independent certified public accountants stating that [counsel] the accountants reasonably believe[s] that no person with a beneficial interest in the account is a restricted person under this Interpretation and stating that, in providing such opinion, [counsel] the accountants:

(1) ha[s]ve reviewed and [is] are familiar with this Interpretation;

(2) ha[s]ve reviewed a current list of all persons with a beneficial interest in the account supplied by the account manager;

(3) ha[s]ve reviewed information supplied by the account manager with respect to each person with a beneficial interest in the account, including the identity, the nature of employment, and any other business connections of such persons; and

(4) ha[s]ve requested and reviewed other documents and other pertinent information and made inquiries of the account manager and received responses thereto, if [counsel] the accountants determine[s] that such further review and inquiry are necessary and relevant to determine the correct status of such persons under the Interpretation.

The member shall maintain a copy of the names and business connections of all persons having any beneficial interest in the account or a copy of the current opinion of counsel in its files for at least three years following the member’s last sale of a new issue to the account, depending upon which of the above requirements the member elects to follow. For purposes of this section, a list or opinion shall be deemed to

be current if it is based upon the status of the account as of a date not more than 18 months prior to the date of the transaction.

Beneficial Interest

The term beneficial interest means not only ownership interests, but every type of direct financial interest of any persons enumerated in paragraphs (1) through (4) hereof in such account, including, without limitation, management fees based on the performance of the account.

Provided, however, that no restricted person shall be deemed to have a beneficial interest in an account receiving a hot issue as a result of ownership of an interest in or the receipt of management fees from an investment partnership or corporation if the following conditions are met.

1. The investment partnership or corporation establishes a separate brokerage account, with a separate identification number, for its new-issue purchases. At the end of each fiscal year, the general partners will certify in writing to its independent certified public accountants that: (a) all hot issues purchased by the partnership were placed in this new-issue account; (b) the partners participating in the new-issue account are not restricted persons under the Interpretation; and (c) that no management fees are based upon the performance of the securities in the new-issue account.

2. Prior to the execution of the initial hot-issue transaction, the partnership’s accountants will provide a certification that complies with paragraph B of the section of the Interpretation entitled “Investment Partnerships and Corporations.”

3. As part of its audit procedure for the partnership, the independent

certified public accountant will confirm in writing to the partnership that all allocations for the new-issue account were made in accordance with the provisions of the applicable partnership agreement that restricts participation in hot-issue purchases.

4. The partnership will maintain in its files copies of the certifications, representations, and confirmations referred to in paragraphs (1) - (3) above for at least three years following the last purchase of a hot issue for the new-issue account.

5. The partnership will accept investment funds from other partnerships if such other partnerships provide the same documentation and assurances described in paragraphs (1) - (4) that restricted persons will not participate in the purchase of hot issues.

6. The certifications and documents required in paragraphs (1) - (3) shall be provided to the member holding such account at such time as these certifications and documents are filed with the partnership and its independent certified public accountant and the member shall make such documentation available to the NASD upon request.

Venture Capital Investors

This Interpretation shall not prohibit the sale of hot issues in an initial public offering to a person enumerated in paragraphs (1) through (4) hereof or to an entity in which such restricted person has a beneficial interest (a "Venture Capital Investor") if the following conditions are met:

1. The Venture Capital Investor has held securities in the company issuing the hot issue securities for a period of one year prior to the effective date of the public offering.

2. The acquisition of the hot-issue securities in the public offering does not increase the percentage equity ownership of the Venture Capital Investor in the company above that held one year prior to the offering.

3. The Venture Capital Investor received no special terms in connection with the purchase.

4. The securities purchased shall be restricted from sale or transfer for a period of six months following the conclusion of the offering.

Violations by Recipient

In those cases where a member or person associated with a member has been the recipient of securities of a public offering to the extent that such violated the Interpretation, the member or person associated with a member shall be deemed to be in violation of Article III, Section 1 of the Rules of Fair Practice and this Interpretation as well as the member who sold the securities since their responsibility in relation to the public distribution is equally as great as that of the member selling them. In those cases where a member or a person associated with a member has caused, directly or indirectly, the distribution of securities to a person falling within the restrictive provisions of this Interpretation the member or person associated with a member shall also be deemed to be in violation of Article III, Section 1 of the Rules of Fair Practice and this Interpretation. Receipt by a member or a person associated with a member of securities of a hot issue which are being distributed by an issuer itself without the assistance of an underwriter and/or selling group is also intended to be subject to the provisions of this Interpretation.

Violations by Registered Representative Executing Transaction

The obligation which members have to make a bona fide public distribution at the public offering price of securities of a hot issue is also an obligation of every person associated with a member who causes a transaction to be executed. Therefore, where sales are made by such persons in a manner inconsistent with the provisions of this Interpretation, such persons associated with a member will be considered equally culpable with the member for the violations found taking into consideration the facts and circumstances of the particular case under consideration.

Disclosure

The fact that a disclosure is made in the prospectus or offering circular that a sale of securities would be made in a manner inconsistent with this Interpretation does not take the matter out of its scope. In sum, therefore, disclosure does not affect the proscriptions of this Interpretation.

Explanation of Terms

The following explanation of terms is provided for the assistance of members. Other words which are defined in the By-Laws and Rules of Fair Practice shall, unless the context otherwise requires, have the meaning as defined therein.

Public Offering

The term public offering shall mean all distribution of securities whether underwritten or not; whether registered, unregistered or exempt from registration under the Securities Act of 1933, and whether they are primary or secondary distributions, including intrastate distributions

and Regulation A issues, which sell at an immediate premium, in the secondary market. It shall not mean exempted securities as defined in Section 3(a)(12) of the Securities Exchange Act of 1934.

Immediate Family

The term immediate family shall include parents, mother-in-law or father-in-law, husband or wife, brother or sister, brother-in-law or sister-in-law, son-in-law or daughter-in-law, and children. In addition, the term shall include any other person who is supported, directly or indirectly, to a material extent by the member, person associated with the member or other person specified in paragraph[s] (2), (3), or (4) above.

Normal Investment Practice

Normal investment practice shall mean the history of investment of a restricted person in an account or accounts maintained with the member making the allocation. In cases where an account was previously maintained with another member, but serviced by the same registered representative as the one currently servicing the account for the member making the allocation, such earlier investment activity may be included in the restricted person's investment history. Usually the previous one-year period of securities activity is the basis for determining the adequacy of a restricted person's investment history. Where warranted, however, a longer or shorter period may be reviewed. It is the responsibility of the registered representative effecting the allocation, as well as the member, to demonstrate that the restricted person's investment history justifies the allocation of hot issues. Copies of customer account statements or other records maintained by the registered representative or the

member may be utilized to demonstrate prior investment activity. In analyzing a restricted person's investment history the Association believes the following factors should be considered:

(1) The frequency of transactions in the account or accounts during that period of time. Relevant in this respect are the nature and size of investments.

(2) A comparison of the dollar amount of previous transactions with the dollar amount of the hot issue purchase. If a restricted person purchases \$1,000 of a hot issue and his account revealed a series of purchases and sales in \$100 amounts, the \$1,000 purchase would not appear to be consistent with the restricted person's normal investment practice.

(3) The practice of purchasing mainly hot issues would not constitute a normal investment practice. The Association does, however, consider as contributing to the establishment of a normal investment practice, the purchase of new issues which are not hot issues as well as secondary market transactions.

Disproportionate

In respect to the determination of what constitutes a disproportionate allocation, the Association uses a guideline 10% of the member's participation in the issue, however acquired. It should be noted, however, that 10% factor is merely a guideline and is one of a number of factors which are considered in reaching determinations of violations of the Interpretation on the basis of disproportionate allocations. These other factors include, among other things:

the size of the participation;
the offering price of the issue;
the amount of securities sold to restricted accounts;
and,
the price of the securities in the aftermarket.

It should be noted that disciplinary action has been taken against members for violations of the Interpretation where the allocations made to restricted accounts were less than 10% of the member's participation. The 10% guideline is applied as to the aggregate of the allocations.

Notwithstanding the above, a normal unit of trading (100 shares or 10 bonds) will in most cases not be considered a disproportionate allocation regardless of the amount of the member's participation. This means that if the aggregate number of shares of a member's participation which is allocated to restricted accounts does not exceed a normal unit of trading, such allocation will in most cases not be considered disproportionate. For example, if a member receives 500 shares of a hot issue, he may allocate 100 shares to a restricted account even though such allocation represents 20% of the member's participation. Of course, all of the remaining shares would have to be allocated to unrestricted accounts and all other provisions of the Interpretation would have to be satisfied. Specifically, the allocation would have to be consistent with the normal investment practice of the account to which it was allocated and the member would not be permitted to sell to restricted persons who were totally prohibited from receiving hot issues.

Insubstantiality

This requirement is separate and distinct from the requirements relating to disproportionate allocations and normal investment practice. In addition, this term applies both to the aggregate of the securities sold to restricted accounts and to each individual allocation. In other words, there could be a substantial allocation to an individual account in violation of the Interpretation and yet be no violation on that ground as to the total number of shares allocated to all accounts. The determination of whether an allocation to a restricted account or accounts is substantial is based upon, among other things, the number of shares allocated and/or the dollar amount of the purchase.

[Interpretation adopted effective November 1, 1970; amended effective January 11, 1972, March 21, 1972, December 1, 1973, June 1, 1983, July 16, 1983 and August 29, 1988].

Sales By Issuers in Conversion Offerings

Definitions

(a) For purposes of this Subsection,

the following terms shall have the meanings stated:

(1) "Conversion offering" shall mean any offering of securities made as part of a plan by which a savings and loan association or other organization converts from a mutual to a stock form of ownership.

(2) "Eligible purchaser" shall mean a person who is eligible to purchase securities pursuant to the rules of the Federal Home Loan Bank Board or other governmental agency or instrumentality having authority to regulate conversion offerings.

Conditions for Exemption

(b) This Interpretation shall not apply to a sale of securities by the issuer on a non-underwritten basis to any person who would otherwise be prohibited or restricted from purchasing a hot issue security if all of the conditions of this Subsection (b) are satisfied.

Sales to Members, Associated Persons of Members and Certain Related Persons

(1) If the purchaser is a member,

person associated with a member, member of the immediate family of any such person to whose support such person contributes, directly or indirectly, or an account in which a member or person associated with a member has a beneficial interest:

(A) the purchaser shall be an eligible purchaser;

(B) the securities purchased shall be restricted from sale or transfer for a period of 150 days following the conclusion of the offering; and

(C) the fact of purchase shall be reported in writing to the member where the person is associated within one day of payment.

Sales to Other Restricted Persons

(2) If the purchaser is not a person specified in Subsection (b)(1) above, the purchaser shall be an eligible purchaser.

[Added effective September 25, 1986.]