



NATIONAL CLEARING CORPORATION

UNIFORM PRACTICE DIVISION *

Attention: Operations Officer, Cashier, Fail-Control Department

September 7, 1973

To: All NASD Members

Re: Shoaf (Cash) & Co., Inc. First Harvard Co.
7 West Campbell Avenue and 55 Liberty Street
Roanoke, Va. 24011 New York, New York 10005

On Wednesday, August 29, 1973 a temporary receiver was appointed for Shoaf (Cash) & Co., Inc. Therefore, members may use the "immediate close-out" procedures under Section 59(i) of the NASD's Uniform Practice Code to close-out open OTC contracts with the firm.

On Thursday, August 30, 1973, a temporary receiver was appointed for First Harvard Co. Previously, members were advised that the "immediate close-out" procedures under Section 59(i) of the Uniform Practice Code could be used to close-out open OTC contracts with First Harvard.

Questions regarding the above-named firms may be directed to:

Firm: Shoaf (Cash) & Co., Inc.
Temporary Receiver:
Frank W. Rogers, Sr.
Woods, Rogers, Muse, Walker & Thornton
105 Franklin S. W.
Roanoke, Va. 24004
Telephone (703) 342-1881

Firm: First Harvard Co.
Temporary Receiver:
Harvey Miller
Weil Gotshal & Manges
767 Fifth Avenue
New York, New York 10022
Telephone (212) 758-7800

Questions regarding this notice may be directed to the Uniform Practice Division of National Clearing Corporation, Two Broadway, 8th Floor, New York, New York 10004, (212) 952-4018.

* The Board of Directors of National Clearing Corporation has been delegated the authority to interpret and enforce the provisions of the Uniform Practice Code pending full implementation of NCC's national clearing system.

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

September 14, 1973

I M P O R T A N T

PROPOSED NEW ENTRY STANDARDS AND REQUIREMENTS FOR REGISTRATION OF PRINCIPALS AND REPRESENTATIVES

TO: All NASD Members and Interested Persons

RE: Proposed New Rules Concerning Standards
for Entry Into The Securities Business

- I. Proposed Amendment to Article I, Section 2
of the By-Laws
- II. Proposed Amendments to Schedule C, Article I,
Section 2 (d) of the By-Laws Concerning
 - (a) Part I - Qualifications and Procedures for being
Admitted to Membership in the Association
 - (b) Part II - Registration of Various Categories of
Principals and Representatives

The Board of Governors of the Association has proposed an amendment to Article I, Section 2 of its By-Laws relating to imposing a bar on officers, partners, principals or controlling persons of a firm in respect to which a SIPC trustee had been appointed if those persons were involved in the activities of the member which led to the appointment of the SIPC trustee, and a variety of amendments to Schedule C, Article I, Section 2 (d) of the By-Laws in which new standards for admission to membership in the Association would be established; certain of the existing requirements would be made more specific; provisions would be made for various categories of registration of principals and representatives and the requirements in respect thereto delineated and, as to certain existing requirements,

made more specific. These proposals, commencing on page 26, are being published by the Board at this time to enable all interested persons an opportunity to comment thereon. Comments on the proposals submitted herewith must be submitted in writing and must be received by the Association by October 15, 1973 in order to receive consideration. After the comment period has expired, the proposals must again be reviewed by the Board. Thereafter, the proposed By-Law amendment must be submitted to the membership for a vote. If approved, it must be submitted to and not disapproved by the Securities and Exchange Commission prior to becoming effective. All Schedule C amendments must also be submitted to and not disapproved by the Securities and Exchange Commission prior to becoming effective.

Explanation of Proposals

The Association has long been concerned with the adequacy of standards for entry into the securities business including those for admission to membership in the Association. This concern became manifested by the fact that in the first two years of the existence of the Securities Investor Protection Corporation (SIPC) approximately 80% of the sixty-four firms who had SIPC trustees appointed were firms which were in business less than five years. Approximately 60% were in existence less than three years. Generally, it can be stated that a predominant reason for many failures has been incompetent and inexperienced management, marginally financed firms and persons of questionable repute being part of management. In this connection many instances have been seen where firms engaged in a given type of business activity with little or no prior experience in that function, such as, trading or underwriting activities, among others. The Association has seen situations where persons who had absolutely no experience or background in any aspect of the securities business organize a broker/dealership which became a member of the Association specifically for the purpose of engaging in an underwriting. They were able to do this merely by themselves passing the appropriate tests for registration and meeting the minimum net capital requirements. The Association does not believe that such ease of entry is conducive to a free, open and orderly market or in the best interests of investors and the public interest.

The historical ease of entry into the securities business and into membership in the Association is a product of the provisions of the Securities Exchange Act of 1934 and the Maloney Act, an amendment thereto, adopted in 1938. The Association, of course, is organized under and operates pursuant to the provisions of the Maloney Act. The language of those statutory enactments expressed the then philosophy of the Congress and the Securities and Exchange Commission that the securities industry should have an open entry policy. This was modified somewhat by the

Securities Acts Amendments of 1964 which amended Section 15A (b) (5) of the Maloney Act and broadened the Association's authority to impose qualifications for membership in the Association. That section states as follows:

The rules of the Association [must] provide that, except with the approval or at the direction of the Commission in cases in which the Commission finds it appropriate in the public interest so to approve or direct, no person shall become a member and no natural person shall become a person associated with a member, unless such person is qualified to become a member or a person associated with a member in conformity with specified and appropriate standards with respect to training, experience, and such other qualifications of such person as the Association finds necessary or desirable, and in the case of a member, the financial responsibility of such member.

This section grants broad authority to the Association to adopt rigid qualification standards for membership. It enables the Association to evaluate membership qualifications on the basis of factors which are much broader than prior to that statutory adoption. Since 1964, the Association has from time to time upgraded its requirements for entry into the securities business and as important and significant as earlier efforts have been, the Association's Board believes they are presently inadequate. The Securities and Exchange Commission has also upgraded standards of entry into the industry by, among other things, increasing minimum capital requirements.

The amendments to the Association's By-Laws and to Schedule C which are enclosed herewith, and explained further below, grow out of the work of two Association committees, the Committee on Entry Standards and the Committee on Qualifications, whose recommendations with certain modifications were accepted by the Board. The Qualifications Committee is an on-going committee of the Association and has been laboring for a considerable period of time to make more clear the requirements for registration of persons with the Association and to develop study material and training guides as well as effective qualifications examinations for those persons. The Committee on Entry Standards was established in January of this year specifically for the purpose of developing more meaningful criteria for entry into membership in the Association given the fact of the large number of failures during the first two years of SIPC's life resulting from inadequate capitalization, inexperienced, incompetent or unethical management, among other things, and the current thinking of the Board of Governors that existing requirements are no longer consistent with the public interest. This Committee has not concluded its work with the package of proposals here presented, however. It is now addressing itself to the more complicated problem of whether procedures similar to those here being proposed as to new members should apply to other situations, i. e., a change in management or a merger, in addition to other

possible business changes. It is anticipated that proposals in respect to such situations will be made by the end of this year.

In respect to entry of a new member into membership in the Association, the program which is embodied in the Schedule C amendments has for its central thrust the restriction of an applicant's business activities in a manner consistent with its capability. Thus, under this program an applicant for membership would not be permitted entry into the Association for the purpose of engaging in trading activities unless it could demonstrate to the satisfaction of the Association that its personnel were capable of and had experience in that business activity. Accordingly, it would not be permitted entry into membership for the purpose of engaging in underwriting activities if it did not have people associated with it skilled in that aspect of the securities business. Thus, the illustration used above of the firm which became a member of the Association with totally inexperienced management and specifically for the purpose of engaging in an underwriting could no longer occur after the adoption of this program.

It must be emphasized that this program does not have for its purpose the denial of membership into the Association; rather, as stated, its purpose is to restrict activities in a manner consistent with the ability of the individuals which make up the management and staff of the applicant firm. Thus, a firm could conceivably be limited, because of the background and experience of its management team, to the distribution of mutual fund shares, only. Also, the qualifications of the individuals associated with the applicant may indicate that the firm is not qualified for membership in the Association. Appropriate due process standards are covered in Sections 4, 5 and 6 of Part I of the proposed revised Schedule C.

Sections 1 and 2 of Part I relate to requirements for principals and financial principals and elaborate upon existing requirements. A new requirement in this respect in Section 1 would be that each of the two principals required before an applicant is granted membership into the Association have at least three years' prior experience with a broker/dealer within the preceding five year period from the date of application for membership and that, functionally, that experience shall have been in a managerial or supervisory capacity during the said three year period. Appropriate exceptions are provided for situations where the business background and experience of an individual justifies that it would not be contrary to the public interest for a member to be admitted notwithstanding the stated experience requirement.

Section 2 contains many new provisions concerning "financial principals" which are already required by the provisions of Schedule C. It should be noted that if an applicant intends pursuant to Section 1 to have only two principals, one of them would have to be a financial principal who would have to meet the experience requirements. Exceptions from such requirements are also provided for depending upon the type of business performed, among

other things. These exception provisions are new and experience under the existing financial principal requirements have dictated such as being necessary. Section 3 of Part I relates to qualified underwriter principals. These provisions have not, however, been included herewith since they were submitted to the membership and interested persons for comment on March 14, 1973 as part of Notice to Members 73-17. In sum, it can be stated that the comments received were not critical and it can be expected that those provisions, with slight modifications, will become part of Schedule C when the entire package submitted herewith becomes effective.

Part II of the proposed new Schedule C relates solely to registration requirements of various categories of persons who are required to be registered. In many respects, the purpose of these amendments is to clarify existing provisions of Schedule C, i. e., making more clear those persons who are specifically required to be registered as principals, financial principals and registered representatives. In the past there have been many questions as to whether certain categories of individuals should be registered as principals. It is believed that the new language will enable the Association and its members to more easily make a judgment since, under the proposals, the category of registration would be premised upon the function performed by the individual rather than the title carried by that individual. Appropriate exemptions would also more clearly be delineated for the benefit of all. Other new provisions are also proposed in connection with registration requirements.

In the first part of the attached package, an amendment to Article I, Section 2 of the By-Laws would impose a bar to registration on certain categories of persons previously associated with a broker or dealer for whom a trustee has been or is subsequently appointed pursuant to the provisions of the Securities Investor Protection Act of 1970 unless the Board of Governors finds it would not be contrary to the public interest to admit that person.

The Association believes this proposed new By-Law provision is required because, as some of the above discussion indicates, so many of the broker/dealers which have ended in a SIPC trusteeship were previously managed by inexperienced or incompetent personnel. Further, the Association has seen instances where individuals have been principals in more than one SIPC-trusted firm. Indeed, situations have been seen where principals have organized an NASD member which had been admitted to membership prior to the time of the demise of the first broker/dealer and the appointment of a SIPC trustee in respect to it. Immediately thereafter, the principals activated the already registered firm and, essentially, continued business as usual. In other cases, a new membership had been

obtained by the principals of the defunct SIPC trustee firm immediately after the appointment thereof and continued business with the new corporate entity. Thus, in each illustration, it was business as usual notwithstanding the previous impact on the public interest and the SIPC fund caused by the principals involved and the potential for such reoccurring. Under the proposals, this would no longer be possible.

A section-by-section analysis of the proposals commences on the following page.

All comments should be addressed to Mr. Donald H. Burns, Secretary, National Association of Securities Dealers, Inc., 1735 K Street, N. W., Washington, D. C. 20006, and should be received by October 15, 1973 in order to receive consideration. All communications will be considered available for inspection.

Sincerely,

A handwritten signature in black ink, appearing to read "Gordon S. Macklin". The signature is written in a cursive style with a long, sweeping underline that extends to the left and then curves back under the name.

Gordon S. Macklin
President

I. Proposed Amendment to Article I,
Section 2 of the By-Laws of the Association

This proposed amendment would redesignate existing subsection (d) of Article I, Section 2, as subsection (e) and insert a new subsection (d), the effect of which would be to prohibit the admission to or continuance in membership in the Association of a broker/dealer who has associated with it a person in the designated categories (officer, director, general partner, owner of ten per centum or more of the voting securities, a controlling person, or a person who was otherwise engaged in any managerial or supervisory capacity) who performed the functions of such with a broker/dealer for whom a SIPC trustee had been or subsequently is appointed unless the Board of Governors of the Association finds that to so admit or continue the member in the Association would not be contrary to the public interest.

Certain criteria are spelled out in the proposal which must be considered by the Board in reaching a determination in such cases. These are: (1) the circumstances surrounding the financial and/or operational difficulties of the broker/dealer for whom the SIPC trustee had been appointed; (2) the involvement of the person associated or to be associated with the broker/dealer in the activities which led to the financial difficulties of the broker/dealer for whom the SIPC trustee had been appointed; and (3) whether it is appropriate in the public interest and for the protection of investors to allow an applicant to be admitted or to be continued in membership with such person associated with it. The Board recognizes that in many cases a person could fall within one of the delineated categories of individuals but yet have had absolutely nothing to do with the activities which led to the demise of the subject firm and the appointment of the SIPC trustee. The amendment, therefore, prohibits the Board from denying membership or the continuance in membership merely because a person falls within one of the listed categories if he had no involvement in the activity which led to the appointment of the SIPC trustee. The amendment specifically states that in such cases admission to or continuance in membership shall be approved.

II. Proposed Amendments to Schedule C, Article I,
Section 2 (d) [to be Redesignated Section 2 (e)] of the By-Laws

Introductory Paragraph

The introductory paragraph makes clear that Schedule C was adopted pursuant to Article I, Section 2 (d) [proposed to be redesignated as Section 2 (e)] of the By-Laws and contains qualifications for membership, requirements for registration with the Association of persons associated with members, and requirements for qualification examinations to be given to

such persons. The Association has been given authority, as quoted above, to establish qualifications for membership pursuant to the provisions of Section 15A (b) (5) of the Maloney Act which also contains specific authority as to individuals. The introductory paragraph also makes clear that where applicable compliance with both Parts I and II of Schedule C must be satisfied before registration with, admission to or continuance in membership in the Corporation will be approved. The net effect of all of these provisions in both Parts I and II is that the granting of admission to membership in the Association will no longer be a perfunctory matter mechanically performed if the minimum statutory requirements, and testing and registration requirements as to individuals, appear to have been met as is necessitated by existing requirements. Rather, affirmative obligations of business responsibility, experience and expertise will be placed upon applicants who will be required to demonstrate such prior to the time they will be permitted to engage in any business activity.

Part I - Qualifications and Procedures
for being Admitted to Membership

Part I of revised Schedule C contains some provisions which appear in existing Schedule C commencing on page 1047 of the Association's Manual. There is much new material, however, concerning new entry standards, establishing pre-admission requirements and granting authority to the staff, District Committees and the Board to evaluate all aspects of an applicant's business to determine whether its planned activities are consistent with the capabilities of the persons it intends to have associated with it. Appropriate due process standards are built in for those situations where an applicant has been denied membership or where restrictions have been placed on the business activities in which it may engage.

Section 1 - Principals; Requirements for Applicants
for Membership and Existing Members

Subsection (a) - This subsection is merely a rewording of the existing requirements of Schedule C prescribing that all applicants for membership in the Association, except of course sole proprietors, must have at least two persons registered as principals before the applicant firm shall be admitted into membership. No substantive changes are being proposed to subsection (a) over existing provisions. Because of the provisions of Section 2 (a), however, if an applicant intends to register only two principals, one of these two would be required to be a financial principal meeting the experience requirements of Section 1 (d) unless the exception provisions of Section 2 (e) applied to the applicant. The experience requirements would

not otherwise be required of a financial principal.

The exception provision for the two principal requirement which is part of existing provisions is contained in proposed subsection (c).

Subsection (b) - This subsection is new and would require that by a date to be determined after effectiveness of the proposals every existing member of the Association, except sole proprietorships, have at least two officers or partners who are registered as principals. This would therefore make universal the requirement of a minimum of two principals per member. Since September 1, 1972, all new members have been required to have two principals. The Board believes it necessary that all firms have at least two qualified principals to provide for those situations where, in one principal firms, the principal may be away from the office or ill or be engaged in some other activity, for whatever reason. With two principals, the void in supervisory and management responsibility would be lessened. It should again be noted that if there are only two principals registered, one of them would be required to be a financial principal because of the provisions of Section 2, unless the exception provisions thereof apply.

Subsection (c) - This subsection contains a waiver provision enabling the President of the Association to waive the subsection (a) or (b) requirements for two principals upon written request and upon it being conclusively demonstrated that only one principal should be required. The President presently has this authority as to applicants for membership. This provision would expand that authority to existing members in view of the new provisions of subsection (b).

Subsection (d) - This new provision would impose an experience requirement on the principals required by subsection (a) as being necessary for admission to membership in the Association. Thus, each of the required two principals would be required to have at least three years' prior experience within the five years immediately preceding the submission of the application for membership in a managerial or a supervisory capacity. The intent behind this provision is that it will have the effect of, or at least take a meaningful step toward, building in some managerial expertise in all new members. The Association's Board recognizes that experience itself does not make a given person competent to perform properly all of the requirements of his office or to have an adequate knowledge of the law, rules and regulations which guide a broker/dealer's activities. Nevertheless, the Board feels it is a measure of protection to the public. Its opinion in this respect is buttressed by the number of firms which have found their way into SIPC trusteeship, discussed above, in the last two and one-half years in which inexperienced or incompetent management has been evident. This requirement does not mean that

all principals must have the "three of five" experience requirement; rather, it means only that the two principals required before admission to membership will be granted must have the requisite experience. After admission to membership has been granted, the new member would be required to keep registered with it as principals two persons meeting the experience requirements.

An exception provision is also included in this paragraph to cover those situations where the business background and experience of an individual justify that permitting registration of that individual would not be contrary to the public interest notwithstanding the lack of conformance with the specific experience requirements of subsection (d). The intent of this exception paragraph is not in any way to dilute the very specific requirement of three years' experience within the preceding five, but is included only to recognize those isolated situations which do surface from time to time where a person of wide and extensive managerial experience, for example, a long time bank president, who may not have had experience directly in the securities business but whose background demonstrates that the public interest would not be adversely affected if he were to become a principal of a new member of the Association. The waiver of the experience requirement would not, however, per se constitute a waiver of requirements to take the Qualification Examination for Principals.

Section 2 - Financial Principals; Requirements for Applicants for Membership and Existing Members

Subsection (a) - Subsection (a) is a rewording of the first sentence of existing Section I (2) (a) (i) of existing Schedule C. The amendment is designed to make clear the intent that at least one financial principal, qualified to become registered as such, is necessary prior to a firm being admitted to membership in the Association unless an exemption has been granted pursuant to subsection (d). A new provision would require that the firm's chief financial officer be a financial principal. Reference should again be made to Section 1 (a) requiring the registration of two principals. As stated above, if only two principals are to be registered, one of them must be a financial principal meeting the experience requirements of Section 1 (d). There is no experience requirement per se for a financial principal, however. In other words, two principals not qualifying as financial principals but meeting the experience requirements of Section 1 (d) could be registered and a third meeting only the requirements of a financial principal could be registered and the applicant would meet the necessary principal requirements for admission to membership assuming, of course, that it did not intend to engage in investment banking activities. In that case, a qualified underwriter principal would be required pursuant to Section 3.

Subsection (b) - This provision makes clear that after an applicant has been admitted to membership in the Association it is not relieved of the requirement to have continuously registered a financial principal. This subsection is a rewording of existing Section I (2) (a) (iii) of Schedule C without any substantive changes.

Subsection (c) - This subsection is new in that it requires every existing member of the Association to designate as financial principals by a date to be specified upon adoption of the proposed amendments all persons associated with it who perform the functions of such as specified in Part II, Section 2 (b). While applicants for membership are required to have a financial principal, there is presently no requirement that existing members have one. The Board believes this inconsistency is not a desirable situation. Under the new proposals, the entire membership would, after the date of effectiveness, be required to have one or more registered financial principals unless they qualified for an exemption under subsection (d).

One of the principals designated to be a financial principal would be required to be the firm's chief financial officer. The principals designated would be responsible for performing the functions of a financial principal after the date of designation. Requirements for the registration of and taking of qualification examinations by such persons would be governed by the provisions of Part II, Section 2 (d) and (e). Generally speaking, persons who were performing the functions of a financial principal (though, of course, not with that title) prior to September 1, 1972 would be grandfathered from the requirements to take a financial principals examination. Other persons would be required to take an examination depending upon their current registration status. The date of September 1, 1972 is significant since it was the effective date of the requirement that new members have a financial principal.

Subsection (d) - This subsection provides an exemption to the financial principal requirements, both as to applicants and existing members of the Association, if the provisions of paragraphs (1) and (2) apply to them. In sum, those provisions relate to the nature of the business activities engaged in by that broker/dealer permitting it to qualify for lower minimum capital requirements under the net capital rule, or for total exemption therefrom. It should be noted that these provisions will be modified to

conform to the provisions of the Commission's proposed uniform capital rule as ultimately adopted.

The purpose behind the subsection (d) provisions relate necessarily to the purpose behind the requirement for a financial principal which is to make certain that every non-exempt firm has a person qualified to properly supervise and/or implement the various financial responsibility rules promulgated pursuant to the Securities Exchange Act of 1934. Because of the nature of their business activities, many firms are not subject to some or all of those provisions. Indeed, some firms by virtue of the nature of their business have been specifically exempted from the provisions of the net capital rule and the recently adopted customer protection rule (Rule 15c3-3 under the 1934 Act).

Section 3 - Qualified Underwriter Principals; Requirements for Membership and Existing Members

As explained in the amended schedule, provisions relating to Qualified Underwriter Principals for new and existing members engaging in an investment banking business (as defined therein) were submitted to the membership and interested persons for comment on March 14, 1973 as part of Notice to Members 73-17. Since those provisions have already been published for comment, they are not being republished at this time. It is anticipated, however, that they will be incorporated into Schedule C with only slight modifications.

Section 4 - Pre-Membership Requirements

Section 4 relating to pre-membership requirements is entirely new. The provisions of Section 4 are the beginning of the new procedures which have the effect of evaluating in detail the proposed plan of business activity of each applicant for membership with the possibility of restrictions upon its business activities being imposed in a manner consistent with its demonstrated capabilities and expertise. Thus, Section 4 relates to pre-membership requirements at the staff level, always in the appropriate District of the Association where the applicant will have its principal place of business, and Section 5 relates to procedures before either the District Committee or the Board of Governors in those situations where an applicant is dissatisfied with the staff judgment of either denial of membership or the imposition of restrictions upon its business activities.

Subsection (a) would require that each applicant for membership at the time it files its application with the Association supply therewith certain

material to the District Office where it has or intends to have its principal place of business including (1) a copy of its business plan which it is required presently to file pursuant to Rule 15b1-2 (c) under the Securities Exchange Act of 1934; (2) a copy of the applicant's written supervisory procedures; (3) a list of all officers, directors, general partners, employees, and any other person who will be associated with the applicant; and (4) any other information or documents which may be deemed necessary in view of the nature of the business activities which the applicant intends to engage in, among other things.

Thus, the initial basic requirement as to all applicants is that great detail in respect to its planned business activities will be required to be filed with the Association prior to the time the application will be approved. It can be assumed that after these requirements become effective, no application will be approved unless each and all of the requirements are met. This is considered essential if the Association is to properly perform its regulatory responsibility and to meet its obligations to investors and the public interest. The Association's Board believes it is inconsistent with its responsibility in those respects to permit membership in the Association to firms who will engage in a business activity totally inconsistent with the capabilities or backgrounds of the persons who are to be associated with it. Indeed, it is possible that when broker/dealers do so they may be, from the first day of their business life, in violation of the well-known fraud-based ^{1/} "shingle theory" which has been spoken to in many SEC and judicial decisions. The onus therefore will be on the applicant firm to demonstrate its capabilities as being consistent with its planned business activities.

Subsection (b) - Subsection (b) would make it mandatory that prior to the time an applicant will be admitted to membership in the Association that the principals required by Sections 1, 2 or 3 will be required to personally appear at the District Office of the District in which the applicant is located for a pre-membership interview. In this connection it is the intent also that even though all of the appropriate documentation has been filed pursuant to Section 4 (a) that an application will not be approved until such time as the prospective member submits to the pre-membership interview at the

^{1/} See Charles Hughes & Co. v. SEC, 139 F. 2d 434 (2nd Cir. 1943) cert. den. 321 US 786, 64 S. Ct. 784 (1944) and many others. This theory, in sum, prescribes that "even a dealer at arm's length impliedly represents when he hangs out his shingle that he will deal fairly with the public", III Loss, Securities Regulation, p. 1483 (2nd Ed. 1961).

Association's District Office in accordance with procedures established by the Association. In effect, each applicant, in accordance with the provisions of this subsection, will be expected to demonstrate at this interview that it has the capability of doing business in the manner which it proposes. In this connection, certain criteria are spelled out in Section 5 (b) upon which the Association must base its determination.

Subsection (c) - This subsection requires that each applicant be notified within thirty days of its pre-membership interview of the results thereof, i. e., whether its application for membership was approved, whether it was denied, or whether it was granted subject to restrictions on the applicant's business activities. It is believed that the thirty day period within which the member must be notified protects the applicant from undue delay, inadvertent or otherwise, on the part of the Association in connection with processing the application. This subsection also prescribes that the determination shall be in writing and shall set forth the specific grounds upon which it is based.

Subsection (d) - This subsection requires that if an applicant accepts the restrictions imposed on its business activities it must execute with the Association prior to approval of membership, an agreement stating that it intends to abide by the restrictions which shall be clearly delineated in the agreement with the reasons therefor. It must agree further that it will not modify or change its business activities in any way inconsistent with such agreement without first notifying and receiving the approval of the Association. This provision is considered necessary. Otherwise, the imposition of restrictions on an applicant's subsequent business activities would be meaningless if it could change them at will. In this connection, it is the intent of the Association to aggressively enforce restrictions imposed and to develop surveillance and regulatory procedures which will make meaningful its efforts in this respect. Procedures for having restrictions relaxed are provided in Section 6 (a) and (b) of the proposals.

Subsection (e) - This provision would provide for an appeal by those persons who have been denied membership or upon whose business activities restrictions have been imposed to the District Committee if such action is taken within fifteen days after receiving notification of the Association's action. Thus, any applicant who is aggrieved by an action of the staff of the Association will have access to the District Committee, that is, to its peers in the business, for an evaluation by them of the applicant's compliance with all admission requirements and its capability to do the kind of business which it has contemplated and which it has indicated it desires to do in its application for membership and in other materials submitted to the Association. This subsection would also make clear that in the case of an applicant who

had restrictions placed upon its business activities it would be permitted to gain membership during the pendency of its appeal to the District Committee, but that its business activities during that period would be restricted in the manner previously imposed. It would first, however, be required to execute the agreement referred to in subsection (d) above. It is also provided that the execution of the agreement would not prejudice any of the applicant's rights on appeal. If denial were the judgment, the applicant would not be admitted pending appeal.

Subsection (f) - This subsection gives a District Committee the authority to call an application for a review on its own motion within twenty days of the staff's notification to an applicant in which case, it is provided, it shall have the authority to stay the effectiveness of any such action if it deems such necessary or appropriate.

Section 5 - District Committees and Board of Governors; Authority and Criteria for Determining Qualifications for Membership; Hearing Procedures

This section contains provisions relating to actions on applications appealed to the District Committee and the Board of Governors and spells out in detail rights of procedural due process which would be accorded to applicants.

Subsection (a) - Subsection (a) conveys authority to each of the various District Committees of the Association to make a judgment as to all applicants whose principal place of business is or will be in the District over which it has jurisdiction as to whether the applicant is qualified for membership, whether it is qualified for membership subject to restrictions on its business activities, either those already imposed or others, or whether it is in the public interest to admit the applicant to membership. Criteria for making such judgment are spelled out in subsection (b). This authority is given to the District Committees in respect to those applications which are before it pursuant to Section 4 (e) or (f), that is, those which have either been appealed by the applicant or which have been called before the Committee for review on its own motion.

Subsection (b) - This subsection, as noted, spells out the criteria upon which the District Committee must base its judgment for admissibility into the Association, for admission subject to restrictions or for a denial of membership. It also provides leeway for a District Committee to make a subjective judgment in other areas where public interest demands such. Thus, initially, the Committee must evaluate factors such as the nature, source and permanence of capital; the applicant's proposed recordkeeping system; its internal procedures, including compliance procedures; and the

capability of the applicant to properly conduct the type of business intended from the standpoint of adequacy; consistency with law and rules of the Corporation; consistency with good business practices and business operations based upon the Committee's experience in the investment banking or securities business; consistency with the applicant's fiduciary obligations to its future customers, and their consistency with the public interest and protection of investors.

It is the Association's view, as noted above, that where such cannot be demonstrated by an applicant it could very well place the applicant in violation of its obligations under the "shingle theory" if it is unable to properly conduct the business in the manner intended. It should be noted further that the capability of an applicant to properly conduct the type of business intended must, according to subsection (b), be evaluated from the standpoint of the number, experience and qualifications of persons associated with or to be associated with the applicant; its facilities; its arrangements with banks and service corporations, or others, necessary to assist it in the conduct of its business; its personnel, methods and procedures for supervision and the conduct of various business activities planned by it, as well as any other factors which may bear on the applicant's ability to conduct an on-going business in an efficient, ethical and legal manner, among other things. These criteria govern also, as noted above, the Association's staff's initial determination as to the appropriateness of the applicant being admitted to membership in the Association for the purpose of performing business in the manner contemplated. These criteria also, pursuant to Section 5 (i) govern the Board of Governors in its determination on an appeal by an aggrieved applicant to it.

Subsection (c) - This subsection provides for procedural due process to an applicant by guaranteeing him the right to appear personally before a District Committee for the purpose of demonstrating its qualifications for membership while doing business in the manner in which it has indicated. This subsection also guarantees an applicant the right to counsel at such a hearing and also prescribes that a record shall be kept of the proceedings and a transcript taken.

Subsection (d) - This subsection prescribes that after the appearance of an applicant, the District Committee shall make its judgment as to admission, denial, or admission subject to restrictions. In addition, it gives it the authority to defer its determination until after admission to it of additional information or documentation deemed by it to be necessary for its determinations. The latter situations undoubtedly will arise infrequently in view of the extensive review of the applicant's plans by the staff prior to the time the application would have gotten to the District Committee level.

Nevertheless, the Board believes a District Committee should have the authority to call for additional information as needed without being bound to a determination on the basis of the hearing if the record is deficient in its opinion.

Subsection (e) - also relates to the District Committee's determination and requires that such be in writing setting forth, in the case of a denial of membership or an acceptance of membership with restrictions, the specific grounds upon which its determination is made. It also requires that the applicant shall be notified of such determination by mail. In practice, this would be done by registered mail with a return receipt requested.

Subsection (f) - This subsection gives all applicants who are aggrieved by an action of the District Committee the right to appeal the District Committee's determination to the Board of Governors within fifteen days from the date of the notice required by subsection (e). It also prescribes what the applicant's status should be during the pendency of such an appeal. In other words, if the District Committee has denied the application, during the pendency of the appeal the applicant shall not be admitted. However, if the applicant had been authorized for admission subject to certain restrictions, it would be admitted to membership and permitted to engage in business in a manner consistent with the restrictions imposed during the pendency of an appeal without such impairing in any way the basis for its appeal. The applicant would, however, be required, prior to the time it would be permitted to engage in business pursuant to such, to execute an agreement with the Corporation in which it acquiesces in and agrees to the restrictions so imposed and agrees further not to change its business activities in a manner inconsistent therewith without first notifying the Association and receiving its approval before admission to and continuance in membership will be declared effective. [See subsection (1)]. If a District Committee or the Board of Governors, pursuant to the appeal modifies the restrictions in any way, its agreement would of course also be required to be modified accordingly. The applicant would therefore be required to re-execute the agreement in a manner consistent with the District Committee's determination for its membership to continue in any manner.

Subsection (g) - This subsection guarantees the right of a hearing to an applicant before a Subcommittee of the Board and also conveys the right to the Board to require a hearing on its own motion if the applicant does not request such if the Board deems it necessary or appropriate. It also permits the applicant to submit any other relevant evidence it desires in addition to that already part of the record and permits representation by counsel. This subsection would also require a record to be kept and a transcript taken.

Subcommittee hearings would proceed in much the same manner as those in disciplinary cases. Thus, a Board Subcommittee would be composed of at least two members, at least one of which would be a current member of the Board of Governors.

Subsection (h) - The hearing Subcommittee, pursuant to subsection (h), would then submit its recommendation to the National Business Conduct Committee at its next meeting which would then, based upon the report made by the Subcommittee of the Board, make a recommendation to the full Board of Governors. All members of the National Business Conduct Committee are current members of the Board and would sit with, and vote with, the Board when it makes its judgment on the application. This is also consistent with procedures followed in disciplinary cases.

This subsection also specifies that either the hearing Subcommittee or the National Business Conduct Committee may supplement the record if such is deemed necessary provided the applicant is given the opportunity to comment on any additional material so introduced prior to a final determination by the Board.

Subsection (i) - Subsection (i) gives the Board of Governors the authority to modify in any way it deems necessary the determination of the District Committee and also prescribes that the criteria spelled out in subsection (b) governing District Committees shall also be applicable to judgments made by the Board of Governors.

Subsection (j) - This subsection provides for notification to the applicant of the Board's determination and requires also that such shall be in writing setting forth the specific grounds upon which the determination is based.

Subsection (k) - Subsection (k) provides for the right of appeal by any person aggrieved by an action of the Board of Governors to the SEC in accordance with Section 15A of the Securities Exchange Act of 1934, as amended.

Subsection (l) - This subsection requires, as noted above, that all applicants upon whose business activities restrictions have been placed execute an agreement with the Association accepting the restrictions so imposed and agreeing further not to change its business activities in a manner inconsistent therewith without first notifying the Association and receiving its approval before admission to and continuance in membership shall be declared effective. It should be noted that the Board is of the opinion that any violation of such an agreement would be grounds for disciplinary

action to be taken pursuant to the provisions of Article III, Section 1 of the Association's Rules of Fair Practice and could result in suspension or expulsion from membership.

Section 6 - Removal of Restrictions

Subsection (a) - Subsection (a) establishes the procedure for the removal of restrictions as to a member if the reasons for the restrictions having been imposed in the first place no longer exist. This authority would be placed in the District Committee for the District in which the member currently has its principal place of business and the onus would be on the member to demonstrate that the factors which gave rise to the imposition of the restrictions have been sufficiently corrected so as to no longer require the continuance thereof for the reasons stated. Criteria to be used by a District Committee in deliberations upon a request for removal of restrictions would be the same as those which the District Committee and the Board of Governors were required to follow in the first instance, i.e., those outlined in Section 5 (b).

Subsection (b) - This subsection guarantees to all applicants for the removal of restrictions the same due process rights guaranteed in the initial proceedings, i.e., those contained in Section 5 (c) through (k).

The Board would like to emphasize that while Sections 4, 5 and 6 contain new procedures and impose more strict qualifications for membership in the Association, at every step of the way an applicant's rights of due process are thoroughly protected and he is given the opportunity to be heard at three levels of the Association, i.e., the staff, the District Committee and the Board of Governors. The Board also believes that these provisions should go a long way toward upgrading the efficiency of management of new members of the Association, especially when coupled with the provisions of Sections 1 and 2 concerning new principal and experience requirements and the requirement concerning financial principals. In this connection, the experience requirements should be helpful and, while by no means a cure-all, should provide meaningful additional assurances of more efficient management because persons who should be more cognizant of their responsibilities to the securities industry and to the public, and who have some managerial background, would be a required part of management of the new member. The provisions will also, therefore, be helpful in assisting in the elimination of those situations where inexperienced or unknowledgeable people inadvertently violate the law or rules without any intent to deceive or defraud the public or other members of the industry.

Part II - Registration Requirements

Section 1 - Registration of Principals

Subsection (a) - This existing subsection would have some minor language changes to make more clear that those persons who function as "principals" must be registered with the Association and that prior to their registration becoming effective, they must pass the Qualification Examination for Principals.

Subsection (b) - contains the definition of principal and is a modification of the language contained in existing Schedule C under Section I (1) (a). The intent is to make clear that anyone engaged in the management, direction or supervision of the day-to-day activities of a member's investment banking or securities business, whoever that person is, shall be registered as a principal. This section spells out certain specific categories of persons including corporate officers and directors, among others, who would be required to be registered as principals. Corporate directors and nominal officers would not be required to register as principals unless they were engaged in the management, direction or supervision of the day-to-day activities of the member's business.

Subsection (c) - This section picks up the "grandfather" clause contained in existing Schedule C making such subject to the provisions of subsection (e) of Section 1. Subsection (e), with one exception, is a restatement of existing language imposing a requirement that a Qualification Examination for Principals be taken in a situation where a principal has been terminated for a period of two or more years immediately preceding the filing of a new application for registration as principal. A new provision would expand this to require the examination where a person has ceased to function as principal for two or more years. Thus, conceivably, though such situations would undoubtedly be rare, if a person had been registered as a principal and engaged in the performance of the functions of such but subsequently, say three years ago, his position was changed and he ceased to perform the functions of a principal and after the expiration of the three years was again assigned principal functions, he could be required by the Association to take a Qualification Examination for Principals. This provision points up the necessity for all members to comply with the requirement that a person's current registration be consistent with the function performed. In other words, if a principal were not currently performing the function of such he should be reclassified and members would have the obligation of notifying the Association of such.

Subsection (d) - Subsection (d) picks up existing provisions of Schedule C and expands upon them in certain respects to make them more specific. Initially, this subsection would, as the current requirements do, prescribe that a person whose duties were changed to that of a principal pass a Qualification Examination for Principal. Presently, however, the applicant is allowed a reasonable time to do so whereas under the proposed subsection he would be required to do so within ninety calendar days following the change of his duties. Also, within ten business days after that change, the member would be required to submit a Principal Elevation Form (PE-3) with the applicable examination fee.

Provisions are also made in this subsection for a situation where the individual during the ninety calendar day period fails the principal's examination. If such occurs, his Form PE-3 will be retained for another ninety day period during which period he could retake the examination without payment of an additional registration fee though an examination fee would have to be paid each time the examination is taken. No person would be permitted to function as a principal beyond the initial ninety calendar day period following the change of his duties without having successfully passed the examination. If a person does not take the examination during the ninety day period immediately following the change of his duties, he would be precluded from taking the examination until such time as he filed a new form and pays the registration and examination fees in connection therewith.

This subsection would also make clear that in no case where a person has not previously been registered in any capacity could he serve as a principal prior to the time he successfully passed the Qualification Examination. Thus, a new applicant for principal status, previously unregistered as a representative, would not be permitted to perform the functions of a principal without first having taken the Qualification Examination for Principal. In this connection, also see Part I, Section 1 (b) imposing a three year experience requirement in the immediately preceding five year period in a managerial or supervisory capacity as being necessary to qualify a person for principal status in certain situations.

Subsection (e) - This was discussed above under subsection (c).

Section 2 - Registration of Financial Principals

Subsection (a) - Subsection (a) would require that all persons who are to perform for a member the duties of a financial principal be registered as such. Before they could be so registered, they would be required to take a Qualification Examination pursuant to subsections (c) or (d) of this Section 2, except as provided in subsection (e).

Subsection (b) - This subsection defines the term "financial principal" as being a person whose duties include, but are not necessarily limited to the various functions delineated therein, including the supervision of performance of the member's responsibilities under all financial responsibility rules promulgated pursuant to the provisions of the Securities Exchange Act of 1934. This definition expands upon the duties in the existing Schedule C which would require a person to be registered as a financial principal.

Subsection (c) - This subsection is a rewording of existing Section I, (2) (a) (ii) of Schedule C. It prescribes that prior to the time an applicant shall be admitted to membership, at least the financial principal designated by it as its chief financial officer must have passed the appropriate examination to qualify him as a financial principal. A new provision would permit, in lieu of Part B of the two-part Qualification Examination for Principals (that part relating to financial principals) as qualifying one for the status of financial principal, an equivalent examination acceptable to the Association. Illustrative of an examination which would be acceptable to the Association is the New York Stock Exchange's financial principals' examination which is currently in the developmental stages. Under this paragraph, therefore, before the applicant could be admitted, at least its chief financial officer would be required to be registered as a financial principal. Other persons could also be so registered. According to the provisions of subsection (a) above, all persons who are to perform the functions of a financial principal would be required to be so registered before they could perform those functions.

Subsection (d) - This subsection would provide the examination requirements for persons designated pursuant to the provisions of Part I, Section 2 (c) to be financial principals who (1) were not previously registered with the Association as principals; and (2) who were previously registered with the Association as principals unless they were covered by the exemptive provisions of subsection (e). In respect to persons not previously registered as principals, this subsection would require that they pass separately within ninety calendar days after their designation Parts A and B of the Principals Examination, or an equivalent examination acceptable to the Association. If persons designated pursuant to Part I, Section 2 (c) were currently registered as principals, they would be required to pass within ninety calendar days only Part B of the Qualification Examination for Principals, or an equivalent examination acceptable to the Association. (See subsection (c) above concerning acceptable equivalent examinations.)

Subsection (e) - This subsection provides the basis upon which persons designated by existing members pursuant to Part I, Section 2 (c) may be exempt from taking Part B of the Qualification Examination for Principals. They would have to meet two requirements as follows: (1) they would have to

have been performing the functions of such prior to September 1, 1972 with the member requesting his registration, and (2) they would have to have been named on a Form MD-1 to be filed with the Association no later than a date to be specified upon the effectiveness of these proposals. It should be noted, therefore, that anyone not listed on a Form MD-1, timely filed on the date required, would not receive the benefits of the exemption. No names would be permitted to be added to Form MD-1 after submission thereof to the Association. Implicit in these provisions is that if a member does not file the completed form by the specified date, all persons performing the financial principal function shall be subject to the examination requirements of subsection (d) before they may become registered as such. Thus, this subsection is really a one-time "grandfather" provision for financial principals. It will operate only once and if not taken advantage of by covered persons at that time, they would lose the benefits thereof. The date of September 1, 1972 is significant in that before that date there was no required registration of financial principals. Since that date, however, such has been required of new members.

Subsection (f) - Subsection (f) is consistent with other provisions relating to registration of persons in that it would require that a financial principal whose most recent registration in that capacity has been terminated for a period of two or more years immediately preceding the filing of a new application, or who has ceased to function as such for a like period, be required to retake the examination for such. This lapse of registration for a two year period has been a long-standing policy of the Association in requiring the retaking of an examination. Requiring such after a similar lapse in functioning as such is new. Members have a responsibility to notify the Association and change the registration of a person who is not functioning according to the category of registration.

Section 3 - Registration of Qualified Underwriter Principals

As explained in the amended schedule, provisions relating to registration of Qualified Underwriter Principals were submitted to the membership and interested persons for comment on March 14, 1973 as part of Notice to Members 73-17. Since those provisions have already been published for comment, they are not being republished at this time. It is anticipated, however, that they will be incorporated into Schedule C with only slight modifications.

Section 4 - Registration of Representatives

Subsection (a) - This subsection contains only minor language changes from the existing provisions.

Subsection (b) - This subsection contains a definition of "representa-

tive" which, with one exception, is the same as that presently contained in Schedule C with certain minor non-substantive language changes. The addition would make certain that those persons designated by a member as having supervisory responsibilities for the firm's compliance with appropriate rules and regulations covering the conduct of its investment banking or securities business would fall within the definition of the term registered representative if not otherwise required to be registered principals. It should be made clear, however, that this does not mean the ultimate responsibility for supervision of such is transferred in any way from those engaged in the management of the member's investment banking or securities business. In this connection it is well established by case law and decisions of the SEC that ultimate responsibility for such is always in management.

The significance of the new provision relating to persons engaged in compliance activities for members is that presently many such persons are not registered. After effectiveness of these proposals, registration of such persons would be required.

Subsection (c) - Subsection (c) relates to the requirement to take an examination upon the lapse of registration for two or more years immediately preceding the date of receipt by the Association of the new application. It is changed only in a clarifying way in that it now specifies that the retaking of the registered representative examination would not be required if the individual had not been registered as such but had been registered continuously with the Association as principal. This has been administrative practice in the past though Schedule C was not clear on this point. The change, thus, is merely clarifying in nature.

Subsection (d) - Subsection (d) (1) relates to the registration with the Association of persons currently registered with SECO. These provisions are, with the exception of certain minor language changes, unchanged from that in existing Schedule C. Subsection (d) (2) relating to the sale of variable contracts also is contained in the existing Schedule C and is modified only in certain minor respects and contains no substantive changes.

Section 5 - Foreign Associates

There have been two changes in this section. One would require a United States office address for the service of process upon a foreign associate, and the other would more positively impose upon the member a responsibility for responding to the Association if the foreign associate cannot be served by the Association.

Section 6 - Persons Exempt From Registration

This section specifying persons exempt from registration is substantially unchanged over the existing exemptive provisions. It does, however,

add a provision requiring the filing of a Form EX-1 in every instance where an exemption is requested or is applicable with the exception of exemptions provided for under subsection (a) (1) or (2) (persons functioning solely and exclusively in a clerical or ministerial capacity and those persons not actively engaged in the investment banking or securities business). Thus, persons desiring to take advantage of all exemptive provisions, or provisions enabling exemption upon application to and approval by the President, with the exceptions noted, must file the required form within ten business days of the date the person becomes associated with the member or the date upon which the exemptive provisions become applicable to him.

Section 7 - Qualification Examinations and Waiver of Requirements

With minor exceptions, this section relating to details of the administration of the Qualification Examination is substantially unchanged over existing provisions. Certain technical changes relating primarily to administration of the provisions are included. The main change would specify in subsection (d) that a person may retake an examination up to three (3) times without any specified time lapse between attempts. However, if a person fails it three times he would thereafter be required to wait ninety days before again taking the examination and between each subsequent attempt. An appropriate examination fee would be required for each attempt. If such is not paid, the subsection specifies that an Admission Certificate would not be issued and proctors would not admit anyone who did not have a proper Admission Certificate.

Section 8 - Confidentiality of Examinations

There have been no changes in this section.

AMENDMENTS TO BY-LAWS

(Page 1046 of the Manual)

- I. Article I, Section 2 of the By-Laws of the Association shall be amended by redesignating subsection (d) thereof as subsection (e) and by inserting in lieu thereof a new subsection (d) as follows:

(d) No broker or dealer shall be admitted to or continued in membership in the Corporation if such broker or dealer has associated with it any person who has been an officer, director, general partner, owner of ten (10) per centum or more of the voting securities, or controlling person of, or was otherwise engaged in any managerial or supervisory capacity with any broker or dealer for whom a trustee has been or is subsequently appointed pursuant to the provisions of the Securities Investor Protection Act of 1970 unless the Board of Governors finds that to so admit or continue a broker or dealer in membership is not contrary to the public interest. The Board of Governors shall consider in reaching a determination in such cases, among other things, the following: (1) the circumstances surrounding the financial and/or operational difficulties of the broker/dealer for whom a SIPC trustee had been appointed; (2) the involvement of the person associated or to be associated with the broker/dealer in the activities which led to the financial difficulties of the broker/dealer for whom a SIPC trustee had been appointed; and (3) whether it is appropriate in the public interest and for the protection of investors to allow a broker/dealer to be admitted to or continued in membership with such person associated with it; provided, however, in those cases where there has clearly been no involvement by the person associated or to be associated with the broker/dealer in the activity which led to appointment of a SIPC trustee, admission to or continuance in membership shall be approved.

SCHEDULE C AMENDMENTS

(Page 1047 of the Manual)

New Material Indicated by Underlining
Deleted Material Indicated by Striking Out

- II. Schedule C of the By-Laws of the Association shall be amended by deleting therefrom subsections (2) and (3) of Section I; by redesignating Sections I through VI as Sections 1 and 3 through 7, respectively, and by redesignating the entire contents thereof as Part II; by adding to the proposed new Part II a new Section 2; by including as the introductory paragraph to Schedule C the existing introductory paragraph of Schedule C, with proposed amendments; and by adding a new Part I, including, among other things, as proposed subsection 1 (a) thereof existing Section (3) of Part I of Schedule C, with proposed amendments, as follows:

SCHEDULE C

This Schedule C has been prepared pursuant to the provisions of Section 2 (e) of Article I of these By-Laws and contains qualification standards for membership in the Corporation and the requirements for registration with the Corporation of persons associated with a member, including requirements for qualification examinations to be given. Where applicable, compliance with the provisions of both Parts I and II of this Schedule must be satisfied before registration with, admission to or continuance in membership in the Corporation will be approved.

Part I - Qualification for Membership

Section 1 - Principals; Requirements for Applicants for Membership and Existing Members

(a) An applicant for membership in the Corporation, except a sole proprietorship, shall have at least two officers or partners who are qualified to become registered as principals pursuant to the provisions of ~~paragraph (1) or (2)~~ Part II hereof, ~~whichever is applicable,~~ before it shall be admitted to membership ~~(b).~~ ~~The President of the Corporation, may in situations which indicate conclusively that only one person associated with a member should be required to register as such, may and upon written request for such waive this requirement. the provisions of this paragraph (3).~~

[Subsection (1) (a) above is a rewording of part of existing Section I (3) of Schedule C. The stricken last sentence appears, as modified, below as subsection (c)].

(b) Every member of the Corporation, except a sole proprietorship, shall by _____ 1973, have at least two officers or partners who are registered as Principals with the Corporation pursuant to the provisions of Part II hereof.

(c) Notwithstanding the provisions of subsections (a) and (b) hereof, the President of the Corporation in situations which indicate conclusively that only one person associated with a member should be required to register as such may upon written request waive the requirements thereof.

(d) Each principal required by subsection (a) hereof shall have at least three years prior experience with a broker/dealer within the preceding five year period from the date of application for membership and shall have functioned with such broker/dealer in a managerial or supervisory capacity during such three year period. After admission to membership, a member shall continue to have at least two principals who meet the requirements of this paragraph. In an exceptional case when the business background and experience of an individual justifies that such would not be contrary to the public interest, the experience requirement herein imposed may upon written request of the individual, and of the member with whom he is to be registered be waived by the President of the Corporation.

Section 2 - Financial Principals; Requirements for Applicants for Membership and Existing Members

(a) Effective September 1, 1972 ~~Every broker and dealer applicant for making application for admission to~~ membership who has not pursuant to the provisions of subsection (d) hereof been granted an exemption from such shall ~~must~~ designate with the Corporation one or more officers or partners, one of whom shall be the firm's chief financial officer, or himself in the case of a sole proprietorship, as Financial Principal who is qualified to become registered as such pursuant to the provisions of Part II, Section 2, hereof.

[Section 2 (a) above is a rewording of the first sentence of existing Section I (2) (a) of Schedule C].

(b) After an applicant has been admitted to membership it must continue to have at least one registered Financial Principal performing the duties of such who has satisfied the requirements of Part II, Section 2, hereof.

[Section 2 (b) above is a rewording of existing Section I (2) (a) (iii) of Schedule C without any substantive changes].

(c) Every member of the Corporation, who has not pursuant to the provisions of subsection (d) hereof been granted an exemption from such shall by _____, 1973 designate as Financial Principal all persons associated with it, at least one of whom shall be the firm's chief financial officer, who perform the functions of such in accordance with the provisions of Part II, Section 2. They shall be registered pursuant to the provisions of Section 2.

(d) A member, or an applicant for membership in the Corporation, may upon written request be exempted by the President of the Corporation from the requirement to have a Financial Principal if:

- (1) it has been expressly exempted by the Securities and Exchange Commission from SEC Rule 15c3-1 pursuant to the provisions of paragraph (b) (3) thereof; or
- (2) it is subject to the provisions of SEC Rule 15c3-1 (a) (3) and (4).

Section 3 - Qualified Underwriter Principals; Requirements for Applicants for Membership and Existing Members

[Section 3 will be reserved for provisions relating to Qualified Underwriter Principals for applicants and members engaging in an investment banking business. Provisions relating to such were submitted to the membership and interested persons for comment on March 14, 1973, as part of Notice to Members 73-17. Since those provisions have already been published for comment they are not being resubmitted at this time].

Section 4 - Pre-Membership Requirements

(a) Each applicant for membership in the Corporation shall at the time application for membership is made furnish to the District Office of the Corporation in which the applicant has or intends to have its principal place of business:

- (1) a copy of the report filed with the Securities and Exchange Commission pursuant to Rule 15b1-2 (c) under the Securities Exchange Act of 1934 and any amendment thereto;
- (2) a copy of the applicant's written supervisory procedures;
- (3) a list of all officers, directors, general partners, employees and any other person who will be associated with the applicant; and
- (4) such other information and documents as may be deemed necessary by the Corporation in view of the nature of the business activities which the applicant intends to engage in, among other things.

(b) Before a broker or dealer shall be admitted to membership in the Corporation the principals of the applicant required by Sections 1, 2 and 3 hereof shall personally appear at the District Office of the District in which the applicant has or intends to have its principal place of business for a pre-membership interview in accordance with procedures established by the Association. At such interview, the applicant shall demonstrate in accordance with procedures established by the Association, the criteria listed in Section 5 (b) hereof, and other factors deemed necessary to the proper conduct of an investment banking or securities business, that it is appropriate in the public interest and not inconsistent with the protection of investors for it to be admitted to membership in the Corporation and to conduct the type of business intended. All documentation submitted in connection with the applicant's application and pre-membership interview shall be made part of the applicant's file for subsequent use on appeal if such occurs.

(c) Within no more than thirty (30) days after such pre-membership interview, the applicant shall be notified by the Corporation whether, consistent with the standards of qualification for membership contained in this Schedule C, including those contained in Section 5 (b) hereof, its application has been granted, denied, or granted subject to restrictions on its business activities. Such determination shall be in writing and set forth the specific grounds upon which the determination is based.

(d) In all cases where restrictions are placed on the business activities of an applicant, the applicant shall, prior to approval of membership by the Corporation, execute an agreement with it accepting and agreeing to abide by the restrictions specified, which with the reasons therefor shall be clearly delineated therein, and agreeing further not to

modify or change its business activities in any way inconsistent with such agreement without first notifying and receiving the approval of the Corporation.

(e) Any applicant whose application for membership has been denied, or upon whose business activities restrictions have been imposed, may appeal such to the District Committee for the District in which it has or will have its principal place of business within fifteen (15) days after the Corporation's action. During the pendency of such an appeal (or a review pursuant to subsection (f) hereof) an applicant upon whose business activities restrictions have been imposed may engage in business in a manner consistent with those restrictions without prejudicing its rights on appeal provided it has executed the agreement required by paragraph (d) hereof.

(f) The District Committee for the District in which the applicant has or will have its principal place of business shall have the right within twenty (20) days after notification to the applicant of the action taken by the Corporation to call the matter before it for review. In such cases, the Committee shall have the authority to stay any prior determination by the Corporation if it deems such necessary or appropriate.

Section 5 - District Committee and Board of Governors;
Authority and Criteria for Determining Qualifica-
tions for Membership; Hearing Procedures

(a) In connection with those applicants before it pursuant to Section 4 (e) or (f) hereof, each District Committee shall have the authority to determine whether an applicant for membership in the Corporation whose principal place of business is or will be within the District over which that District Committee has jurisdiction, is qualified for membership in the Corporation, whether it is qualified for membership pursuant to restrictions on its business activities, either those previously imposed by the Corporation or others, and whether in any event it is in the public interest to admit the applicant to membership in the Corporation.

(b) A District Committee in reaching its determination as to the qualifications of an applicant for membership in the Corporation, or whether it is qualified pursuant to restrictions being placed upon its business activities, shall review and consider each of, but not necessarily only, the following factors of the applicant's business plans to determine as to each, in view of the type of business to be engaged in, their adequacy; their consistency with law and the rules of the Corpora-

tion; their consistency with good business practices and business operations based upon the Committee's experience in the investment banking or securities business; their consistency with the applicant's fiduciary obligation to its future customers, and their consistency with the public interest and the protection of investors:

- (1) The nature, source and permanence of the capital of the applicant and the sources of and arrangements for additional capital in case a business need arises;
- (2) The applicant's proposed recordkeeping system;
- (3) The applicant's proposed internal procedures, including compliance procedures, from the standpoint of insuring to the extent possible adherence to all applicable laws, rules and regulations; and
- (4) The capability of the applicant to properly conduct the type of business intended in view of the:
 - a. number, experience and qualifications of the persons associated with or to be associated with the applicant;
 - b. facilities which the applicant contemplates having;
 - c. arrangements, if any, with banks and clearing corporations, or others, to assist the applicant in the conduct of its securities business;
 - d. personnel, methods and procedures intended for the supervision of persons associated with the applicant and the conduct of the various business activities planned by it; and
 - e. any other factors which may bear on the applicant's ability to conduct an on-going business in an efficient, ethical and legal manner; in a manner consistent with its fiduciary obligation to its future customers, and in a manner consistent with the public interest.

(c) In connection with an application before a District Committee pursuant to Section 4 (e) or (f) hereof, an applicant for membership in the Corporation shall have the right to appear personally before the District Committee to demonstrate its qualifications for membership

and to be represented by counsel. A record shall be kept of the proceedings and a transcript shall be taken.

(d) The District Committee, after appearance of the applicant and consideration of its qualifications for membership shall, notwithstanding action previously taken by the Corporation, accept or deny admission of the applicant to membership in the Corporation, or accept the applicant for admission to membership with restrictions on its business activities as deemed appropriate by the Committee, or defer its determination until after submission to it of additional information or documentation deemed by it to be necessary to its determinations.

(e) The applicant, or a member, shall be notified by mail of the determination of the District Committee. The District Committee's determination shall be in writing and shall set forth, in the case of a denial of membership or an acceptance of membership with restrictions, the specific grounds upon which its determination is made.

(f) All actions of a District Committee in respect to applicants for membership in the Corporation shall be subject to review by the Board of Governors upon application by the applicant for membership filed within fifteen (15) days after the date of notice required by subsection (e) hereof. Upon application to the Board of Governors for review in a case where the District Committee has denied an applicant membership in the Corporation, the applicant shall not be admitted to membership during the pendency of proceedings before the Board of Governors. When admission has been granted subject to restrictions upon an applicant's business activities, the applicant shall be admitted to membership pursuant thereto and will be permitted to engage in business in a manner not inconsistent therewith during the pendency of the appeal without prejudice to any of his rights of appeal if it agrees first to and does execute an agreement with the Corporation in accordance with the provisions of subsection (1) hereof.

(g) In an application for review pursuant to subsection (f) hereof, the applicant may request a hearing before a Subcommittee of the Board of Governors. In the absence of such request for hearing, the Board of Governors may require a hearing on its own motion if it deems such action necessary or appropriate. At such hearing the applicant may submit such other relevant evidence, in addition to that already part of the record, which it desires and it shall be entitled the right to be represented by counsel. A record shall be kept of the proceedings and a transcript shall be taken.

(h) The recommendation of the Subcommittee of the Board will then be submitted to the National Business Conduct Committee at its next meeting which, after review of the matter, will decide upon a recommendation to be made to the Board of Governors. The recommendation of the National Business Conduct Committee will then be submitted to the Board of Governors for its action at its next meeting. The hearing Subcommittee of the Board (or the National Business Conduct Committee or the Board itself, as the case may be) shall have the right to supplement the record if such is deemed necessary provided the applicant is given the opportunity to comment on such supplementary material prior to a final determination by the Board.

(i) In any proceeding to review any action taken by a District Committee, the Board of Governors, upon consideration of the record before it, may modify such action as it deems necessary or appropriate considering the criteria stated in subsection (b) hereof which criteria shall also govern determinations of the Board of Governors.

(j) An applicant shall be notified of any determination of the Board of Governors on an application for review of any action taken by a District Committee. Such determination shall be in writing and set forth the specific grounds upon which its determination is based.

(k) In any case where the applicant feels aggrieved by any action taken by the Board of Governors, it may make application for review to the Securities and Exchange Commission in accordance with Section 15A of the Securities Exchange Act of 1934, as amended.

(l) In any case where restrictions have been placed upon the business activities of an applicant by the Board of Governors or a District Committee, the applicant shall prior to approval of membership be required to execute an agreement with the Association acquiescing in and agreeing to the restrictions so imposed and agreeing further not to change its business activities in a manner inconsistent therewith without first notifying the Association and receiving its approval before admission to and continuance in membership will be declared effective.

Section 6 - Removal of Restrictions Imposed

(a) Any restrictions on the business activity of an applicant may subsequently be removed by the District Committee for the District in which the member currently has its principal place of business, unless the member has removed its principal of business to another District whereupon they may be removed by the District in which it currently

has its principal place of business, upon an appropriate showing by the member that the factors which gave rise to the imposition of the restrictions have been sufficiently corrected so as to no longer require the continuance of the restrictions for the reasons stated. In doing so, a District Committee shall consider the record which gave rise to the imposition of the restrictions and the criteria governing its determinations contained in Section 5 (b) hereof as well as any supplement thereto submitted in connection with the request for removal of the restrictions.

(b) A member who has requested the removal of restrictions pursuant to Section 6 (a) hereof shall be entitled to all of the procedural rights spelled out in Section 5 (c) through (k) hereof.

Part II - Registration Requirements

I.

Section 1 - Registration of Principals

(1) (a) Registration Requirements

All persons associated with a member who ~~are designated~~ are to function as Principals must be registered as such with the Corporation. ~~and must pass a Qualification Examination for Principals before~~ Before their registration can become effective, they must pass the Corporation's Qualification Examination for Principals.

(b) Definition of Principal

The term "principal" shall mean a persons associated with a member, ~~enumerated in (i) -- (v) hereafter,~~ who is ~~are~~ actively engaged in the management, direction or supervision of the day-to-day activities of the member's investment banking or securities business. ~~including supervision, solicitation, conduct of business or the training of persons associated with a member for any of these functions, are designated as Principals.~~ Such persons shall include, but not necessarily be limited to:

(i) (1) Sole Proprietors;

(ii) (2) Corporate Officers and Directors who manage, direct, or supervise the day-to-day investment banking or securities business of the member;

~~(iii)~~ (3) Partners; and

~~(iv)~~ (4) Managers of Offices of Supervisory Jurisdiction,
and

~~(v)~~ Directors of Corporations.

(c) Grandfather Clause

Any person who was registered with the Corporation on or before October 1, 1965, and designated as a Sole Proprietor, Officer, Partner, Manager of Office of Supervisory Jurisdiction or Director is not required to pass a Qualification Examination for Principals, subject to the provisions of ~~paragraph-(d)-(6)~~ subsection (e) hereof.

(d) Elevation to Principal Status

Any person associated with a member as a Registered Representative whose duties are changed ~~by the same member after~~ October 1, 1965, so as to require his Principal classification as a Principal shall within ten (10) business days thereof submit a Principal Elevation Form (PE-3), with the applicable examination fee. The applicant will be allowed a reasonable period of time 90 calendar days following such a the change in his duties during which to pass a Qualification Examination for Principals. If the applicant fails the examination, the Elevation form and application will be retained for an additional period of 90 calendar days from the date of the last failure. If the applicant fails to take the examination within the initial 90 calendar day period, a new Principal Elevation form and examination fee will be required. In no event may such person function as a Principal beyond the initial 90 calendar day period following the change in his duties without having successfully passed the examination. In no event may a person previously unregistered in any capacity applying for Principal status function as a Principal until fully qualified.

(e) Requirement for Examination on Lapse of Registration

Any Principal whose most recent registration as a Principal has been terminated, or who has ceased to function as such, for a period of two years or more years immediately preceding the filing of a new application for registration as a Principal shall be required to pass a the current Qualification Examination for Principals.

Section 2 - Registration of Financial Principals

[Note: This Section 2 replaces existing Section I (2) of Schedule C and contains a number of substantive changes].

(a) Registration Requirements

All persons associated with a member not exempted by Part I, Section 2 (d) from the requirement to have a Financial Principal who are to perform the duties of a Financial Principal must be registered as such with the Corporation except as hereinafter provided. Before their registration can become effective they shall be required, unless otherwise provided, to pass a qualification examination in accordance with the provisions of subsections (c) or (d) hereof.

(b) Definition of Financial Principal

The term Financial Principal shall mean a person associated with a member whose duties include, but are not necessarily limited to:

- (1) final approval and responsibility for accuracy of financial reports submitted to any duly established securities industry regulatory body;
- (2) final preparation of such reports;
- (3) supervision of individuals who assist in the preparation of such reports;
- (4) supervision of and responsibility for individuals who are involved in the actual maintenance of the firm's books and records from which such reports are derived; or
- (5) supervision and/or performance of the member's responsibilities under all financial responsibility rules promulgated pursuant to the provisions of the Securities Exchange Act of 1934.

(c) Examination Requirement for Financial Principal of Applicant for Membership

Before an ~~broker or dealer~~ applicant which has not been granted an exemption pursuant to the provisions of Part I, Section 2 (d) shall be

admitted to membership in the Corporation, at least the designated Financial Principal who is the firm's chief financial officer shall ~~must~~ pass or have passed separately ~~Parts I and II~~ Parts A and B of a ~~two-part~~ the Qualification Examination for Principals, or an equivalent examination acceptable to the Corporation, unless he is currently qualified to be registered as a Principal pursuant to ~~paragraph (1) hereof~~ in which case he must pass ~~Part II~~ Part B, only, of that examination, or an equivalent examination acceptable to the Corporation.

[Subsection (c) above is a rewording of existing Section I (2) (a) (ii) of Schedule C without any substantive changes].

(d) Examination Requirements for Financial Principals of Existing Members

Except as provided in subsection (e) hereof, any person required by the provisions of Part I, Section 2 (c) to be designated as a Financial Principal who was not previously registered with the Corporation as a Principal must pass separately within 90 calendar days of the date of designation as such, Parts A and B of the Qualification Examination for Principals, or an equivalent examination acceptable to the Corporation. If such person is currently registered with the Association as a Principal, he shall be required to pass within 90 calendar days of the date of designation Part B of the Qualification Examination for Principals, or an equivalent examination acceptable to the Corporation.

(e) Exemption from Requirement to Take Financial Principal Examination

Principals designated pursuant to the provisions of Part I, Section 2 (c) hereof shall not be required to take Part B of the Qualification Examination for Principals if:

- (1) such person had been performing a Financial Principal function as defined in subsection (b) hereof on or before September 1, 1972 with the member requesting this registration; and
- (2) such person is named on Form MD-1 which shall be filed with the Corporation no later than the close of business _____ 1973; provided, however, that a person listed on Form MD-1 who is not currently

registered as a Principal shall be required within 90 calendar days of the filing thereof with the Corporation to pass Part A of the Qualification Examination for Principals before becoming registered as a Financial Principal, previous exemption from registration since October 1, 1965 notwithstanding.

(f) Requirement to Retake Examination
Upon Lapse of Registration

A Financial Principal whose most recent registration in that capacity has been terminated for a period of two years or more immediately preceding the filing of a new application, or who has ceased to function as such for that period, shall be required to pass Parts A and B of the Qualification Examination for Principals, or only Part B if during that period its registration as a Principal remained effective and he continued to perform the functions of a Principal.

Section 3 - Registration of Qualified Underwriter Principals

[Section 3 will be reserved for provisions relating to the registration of Qualified Underwriter Principals. Provisions relating to such were submitted to the membership and interested persons for comment on March 14, 1973, as part of Notice to Members 73-17. Since those provisions have already been published for comment they are not being resubmitted at this time].

II.

Section 4 - Registration of Representatives

(a) Registration Requirements

All persons associated with a member who are designated to function as Registered Representatives must be registered with the Corporation and must pass ~~an Association~~ the Corporation's Qualification Examination for Registered Representatives before their registration can become effective.

(b) Definition of Representative

~~Employees~~ The term Representative shall mean a person associated with a member, including assistant officers other than Principals,

who are engaged in the investment banking or securities business for the member. Such persons shall include, but not necessarily be limited to, those persons engaged in the supervision, solicitation or conduct of business in securities; ~~who are persons~~ engaged in the training of persons associated with a member for any of ~~these~~ those functions; ~~are designated as Representatives.~~ and those persons designated by a member as having supervisory responsibility for the firm's compliance with any governmental agency, or supervisory persons who devote a significant amount of time thereto, if such persons are not otherwise required to be registered as principals.

(c) Requirement for Examination on Lapse of Registration

Any Registered Representative whose most recent registration as such has been terminated for a period of two years or more years immediately preceding the filing date of receipt by the Association of a new application shall be required to pass a Qualification Examination for Representatives unless he has been continuously registered with the Association as a Principal.

(d) Special Situations

(1) Current Registration with SECO

- a. Persons associated with a member who are currently qualified to engage directly or indirectly in securities activities with a non-member broker/dealer as a result of having taken and passed an examination pursuant to the provisions of Section 15 (b) (8) of the Securities Exchange Act of 1934, as amended, and Rule 15b8-1 thereunder, more commonly known and hereafter referred to as the SECO examination, or were not required to take the SECO examination because of the exemption provided in Rule 15b8-1, for persons who were broker/dealers or became associated persons prior to July 1, 1963, and have been continuously registered as such since that date shall not be required in order to become registered as a Representative of a member of the Corporation to take and pass the general securities section of the Qualification Examination for Registered Representatives provided for in subsection (a) (1) hereof unless he has been terminated with the non-member broker/dealer for two or more years.

All such persons shall, however, be required to take and pass an examination based on the Corporation's rules and regulations before he may function as a Registered Representative with a member.

- b. Persons associated with a member who have not taken the SECO examination but who have become and are currently qualified pursuant to the provisions of Section 15 (b) (8) of the Securities Exchange Act of 1934, as amended, and Rule 15b8-1 thereunder, as a result of acceptance by the Securities and Exchange Commission of a securities examination administered by and for a state securities administration, and successfully completed by the applicant, shall be required, unless that state's examination is also accepted by the Corporation, to take the Qualification Examination for Registered Representatives unless he has been fully registered pursuant to the referred to Section 15 (b) (8) and Rule 15b8-1 for at least one year immediately preceding the date of receipt of his application with by the Corporation. All such persons who are ~~exempt from taking~~ not required to take the Qualification Examination for Registered Representative because of the one year experience factor shall, however, be required to successfully complete an examination based upon the Corporation's rules and regulations before he may function as a Registered Representative with a member.

(2) Sale of Variable Contracts Only

- a. All persons associated with a member who are included within the scope of the categories contained in subsection (1) (a) of this Section 4 but whose activities in the investment banking and or securities business are limited solely to investment contracts known as variable contracts, must either qualify as Registered Representatives pursuant to the provisions of subsections (a) or (d) (1) hereof, or ~~pass or have previously passed~~ prior to July 1, 1970 have successfully completed a general securities examination prepared and approved by the National Association of Insurance Commissioners, ~~plus~~ In addition, an examination on the Corporation's rules and regulations must also be completed successfully before their registration can become effective. A person so

qualifying shall be ~~designated~~ registered as a REGISTERED REPRESENTATIVE FOR SALE OF VARIABLE CONTRACTS ONLY.

- b. Any ~~registered representative for sale of variable contracts only~~ REGISTERED REPRESENTATIVE FOR SALE OF VARIABLE CONTRACTS ONLY ~~whose most recent registration~~ or persons whose qualification to sell variable contracts only pursuant to the provisions of Section 15 (b) (8) of the Act and Rule 15b8-1 thereunder ~~to sell variable contracts only~~ whose most recent registration has been terminated for a period of two years or more immediately preceding the filing date of receipt of his application by the Corporation, shall be required to again qualify before his registration pursuant to ~~subparagraph (2) (b) (2)~~ this subsection (d) (2) can become effective.

∇.

Section 5 - Foreign Associates

(a) Exemption from Registration and Qualification Examination

All persons associated with a member who are ~~designated to function~~ as Foreign Associates shall not be required to be registered and shall be exempt from the requirement to pass a Qualification Examination. ~~Persons associated with a member shall be designated as Foreign Associates if they meet the following criteria:~~

(b) Definition of Foreign Associate

The term "foreign associate" shall mean a person associated with a member:

- (1) ~~They are~~ who is not a citizen, national, or resident of the United States or any of its territories or possessions; and
- (2) ~~They who~~ will conduct all of ~~their~~ his securities activities in areas outside the jurisdiction of the United States and ~~they~~ will not engage in any securities activities with or for any citizen, national, or resident of the United States.

(c) Requirement of Application for Foreign Associate

Prior to the time the exemption provided for in ~~this paragraph~~ subsection (a) hereof may become effective, the member desiring to employ any such person must file with the Corporation, a form designated "Application for Classification as a Foreign Associate" for each such person and must certify that such person meets the above two criteria contained in subsection (b) hereof as well as that:

- (1) ~~(3)~~ Such person is not subject to any of the prohibitions to registration with the Corporation contained in Article I, Section 2 (a) through 2 ~~(c)~~ (d) of the By-Laws of the Corporation; and
- (2) ~~(4)~~ Service of process for any proceeding instituted by the Corporation in respect to such person may be sent to an address ~~designated by the member in the~~ United States at an office of the member. The member will be responsible for responding to the Association if the individual cannot be served.

(d) Termination of Employment

~~Further,~~ In the event of termination of the employment of a Foreign Associate, the member must notify the Corporation immediately by filing a notice of termination as required by Article XV, Section 5 of the By-Laws.

~~III.~~

Section 6 - Persons Exempt From Registration

(a) The following persons associated with a member are not required to be registered with the Corporation:

- (1) Persons associated with a member whose functions are solely and exclusively clerical or ministerial.
- (2) Persons associated with a member who are not actively engaged in the investment banking or securities business.
- (3) Persons associated with a member whose functions are related solely and exclusively to the member's need for

nominal corporate officers or for capital participation, as in the case of limited partners.

(4) Persons associated with a member whose functions are related solely and exclusively to:

(a) a. transactions on a registered national securities exchange and who are registered with such exchange; or,

(b) b. transactions in exempted securities; or,

(c) c. transactions in commodities.

(b) In every instance where exemption is requested or applicable, except pursuant to the provisions of subsection (a) (1) or (2) hereof, the member must file Form EX-1 with the Association within ten (10) business days of either the date the person becomes associated with the member or the date on which the exemptive provisions become applicable to him.

IV.

Section 7 - Qualification Examinations and Waiver of Requirements

(a) Study Outline

(1) Qualification Examinations for Principals, Financial Principals and Registered Representatives shall consist of a series of questions based upon topics outlined in the document entitled "Study Outline for Qualification Examinations for Registered Representatives and Registered Principals". ~~Qualification Examinations for Registered Representatives shall consist of a series of questions based upon topics outlined in the document entitled "Study Outline for Qualification Examinations for Registered Representatives and Registered Principals".~~

(b) Time and Place

(2) Examinations shall be given at such times and places and under such conditions as shall be prescribed by the Board of Governors and shall be graded according to the procedure prescribed by the Board of Governors.

(c) Grading Scale

(3) Examination results shall be reported by one of the following letter grades: A (Excellent), B (Good), C (Fair), or F (Failed). Scores assigned to each letter grade for each examination series shall be determined by the Board of Governors.

(d) Procedure Upon Failing Examination

Applicants who fail an examination may, subject to the payment of required examination fees and receipt of a new Admission Certificate, retake such examination up to three times without waiting any specified period of time between attempts. If an examination is failed three (3) times, the applicant must wait 90 days before again taking the examination, and between each subsequent attempt. A new Admission Certificate will not be issued in connection with any examination until proper fees for the examination have been received by the Corporation. Proctors will admit only those candidates having a valid Admission Certificate.

(e) Assistance During Examination

Each applicant shall certify to the Board of Governors that no assistance was given to or received by him during the examination.

~~(4) The President of the Corporation may, in exceptional cases and where good cause is shown, waive the applicable Qualification Examination upon written request by the member, and accept other standards as evidence of an applicant's qualifications for registration. Advanced age, physical infirmity or experience in fields ancillary to the investment banking or securities business will not individually or themselves constitute sufficient grounds to waive a Qualification Examination.~~

(f) SECO Grace Period

(5) The President of the Corporation, or his delegate, in the case of a broker/dealer applicant for membership in the Corporation who was previously qualified, and at the time of his application for membership is currently qualified, pursuant to the provisions of Section 15 (b) (8) of the Securities Exchange Act of 1934, as

amended, and Rule 15b8-1 thereunder, shall have the discretion to grant a grace period of reasonable and stated duration after the effective date of membership of the applicant, during which period of time the persons associated with the member who were previously, and at the time of their applications are, qualified pursuant to the aforementioned Section 15 (b) (8) and Rule 15b8-1 may actively engage in the investment banking and or securities business while qualifying as Registered Representatives and Principals; provided, however, the provision of this subsection shall in no way be construed so as to contravene the minimum qualifications for membership in respect to Principals required pursuant to the provisions of Part I, Sections 1, 2 or 3 of this Schedule C. ~~pursuant to the provisions of this Schedule C.~~ In no event may the said grace period exceed one year from the effective date of membership of the applicant. If the referred to persons associated with the member do not qualify, pursuant to Schedule C, by the date of the expiration of the grace period, they shall no longer be permitted to engage in the investment banking and or securities business until they qualify thereunder. In no case shall a person not currently qualified under Section 15 (b) (8) and Rule 15b8-1 be permitted to act as a Representative or any category of Principal of the member during the grace period unless he has qualified pursuant to the provisions of Schedule C.

(g) Waivers

(1) In exceptional cases and where good cause is shown the President of the Corporation, or his delegate, upon request by the member may waive the requirement to take an applicable Qualification Examination. All such requests shall be in writing, addressed to the President of the Corporation, and signed by a registered Principal of the requesting firm.

(2) Advanced age, physical infirmity, experience in fields ancillary to the investment banking or securities business will not individually of themselves constitute sufficient grounds to waive a Qualification Examination.

(3) A request for waiver based on the expiration of the two year period since the most recent registration with the Association will not be honored.

(4) No extension of time will be granted for taking Qualification Examinations beyond that specified within this Schedule. Except

where otherwise specified therein, required Qualification Examinations must be taken and passed by the candidate and the member notified by the NASD prior to the individual commencing to perform the function for which he is seeking registration.

v.

Section 8 - Confidentiality of Examinations

The Corporation considers all of its Qualification Examinations to be highly confidential. The removal from an examination center, reproduction, disclosure, receipt from or passing to any person, or use for study purposes of any portion of such Qualification Examination, whether of present or past series, or any other use which would compromise the effectiveness of the Examinations and the use in any manner and at any time of the questions or answers to the Examinations are prohibited and are deemed to be a violation of Article III, Section 1 of the Rules of Fair Practice.

NASD

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

September 19, 1973

TO: Select NASD Members
Attention: Members effecting business in exempted securities

RE: Exempted Security Questionnaire

On April 10, 1973 the Securities and Exchange Commission announced the indefinite extension of the temporary suspension of the requirements of paragraph (m) of SEC Rule 15c3-3 with regard to transactions in exempted securities. ^{1/} Paragraph (m) of the rule requires that a broker-dealer close out customer sale transactions by purchasing securities of like kind and quantity when the securities sold by the customer have not been physically obtained by the broker-dealer within ten business days past settlement date. The Commission based its suspension on representations received at or about the time of the implementation of the rule in January 1973 that operational hardships may possibly arise or result from attempts to buy-in exempted securities, particularly municipal obligations, within the designated time frames of paragraph (m).

Coinciding with this development, the Association and the major national securities exchanges were requested to gather data to assist the Commission in its determination of the extent of problems associated with the failure by customers, financial institutions, banks, exempt dealers or broker-dealers to make timely settlements of transactions in exempted securities.

Subsequently through the coordinated efforts of the various self regulators and Commission staff a standardized form to be used in gathering the needed data was developed. In this connection, the Association was asked to collect this data for this limited purpose report for all members who are not members of the NYSE. The NYSE has been requested to collect the data from its membership, and all other registered national securities exchanges have been requested to collect the data from their respective sole members.


^{1/} See Securities Exchange Act Release No. 10093, dated April 10, 1973 and NASD Notice to Members No. 73-37 dated April 9, 1973.

With respect to the above, enclosed please find four copies of the questionnaire which you are asked to complete, reflecting month-end balances, by the 10th of each month for four consecutive months. The initial report is to be completed and returned to the NASD by October 10th, 1973 for month ending September 1973. The three (3) remaining questionnaires for the months ending October, November and December, 1973 should be completed and returned by the 10th of each following month.

Your cooperation in this matter is essential since the data will be the basis of the Commission's determination of whether such suspension of the application of paragraph (m) as to exempt securities should continue or whether other measures are appropriate.

Any questions regarding this questionnaire or related matters should be directed to Robert L. Smith at (202) 833-7356.

Sincerely,

A handwritten signature in cursive script, appearing to read "Frank J. Wilson".

Frank J. Wilson
Senior Vice President
Regulation

EXEMPT SECURITY QUESTIONNAIRE

Date: _____

Period: _____

Member Name and Address

(No. and Street)

(City)

(State)

(Zip Code)

Member of: NYSE AMEX Pacific Midwest Boston PBW NASD Detroit Cinci Other: _____

1. The number of contracts for exempt* securities in **Fail to Receive** at month end with other brokers or dealers for
 a) 10 calendar days or less, b) over 10 but less than 31 days, c) over 30 days.

# of Contracts	Calendar Days	Aggregate Value \$***
	10 days or less	
	over 10, less than 31 days	
	over 30 days	
	Total	

2. The number of customers [include banks, individuals, etc.] who, with respect to exempt securities, have not delivered such securities sold as defined in paragraph (m) of 15c3-3 for
 a) 10 business days or less, b) over 10 but less than 31 days, c) over 30 days.

# of Customers	Business Days	Aggregate Value \$***
	10 days or less	
	over 10, less than 31 days	
	over 30 days	
	Total	

3. Total number and value of Trades involving the **sale** of exempt securities entered into since the period covered by previous report by

(First report should cover period since previous month end.)

	# of Trades	Aggregate Value \$***
a) Customers		
b) Broker-Dealers		

4. Methods employed, other than in accordance with the provisions of the sales contract, to close out trades reported in question 3 above.

	Buy In	Cancel	Other	Total
a) Customers	#	#	#	#
	\$	\$	\$	\$
b) Broker/Dealers	#	#	#	#
	\$	\$	\$	\$

5. Provide schedule for each category in item #4 above for age ** of all contracts settled or closed out.
Example: 2 @ 12 days, 5 @ 40 days, etc.

6. a) Name and title of person completing questionnaire :

b) Name and title of partner or officer reviewing questionnaire :

(if different from above):

c) Phone number of firm :

NOTES

* For purposes of this questionnaire, exempted securities shall be those securities, as defined in Section 3(a)(12) of the 1934 Act.

** Aging begins with settlement date.

*** At contract price.

Complete and return by the 10th of the month to:

National Association of Securities Dealers, Inc.
Department of Regulatory Policy and Procedures
1735 K Street, N.W.
Washington, D. C. 20006

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

September 19, 1973

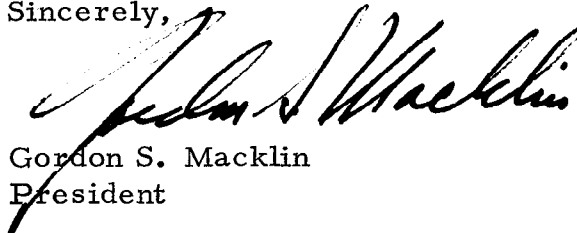
To All NASD Members:

The Securities Investor Protection Corporation (SIPC) has advised the Association that certain member broker/dealers have not been cooperative with SIPC trustees where such is required because of outstanding fails, contractual commitments or other matters.

The Association's Board of Governors believes that cooperation with SIPC trustees by broker/dealers is essential to the proper conduct of their investment banking or securities business and that such is in the best interests of all members and the public. Cooperation is also necessary if the trustees are to perform properly their functions under the law and to enable as promptly as possible the payout of customers' funds or delivery of customers' securities. You are undoubtedly aware that there has recently been some criticism as to the time it has taken trustees to make these payments and deliveries. Cooperation by brokers would undoubtedly materially assist in expediting this process.

Accordingly, the Board of Governors has adopted a resolution requiring all members to cooperate fully with all trustees appointed under the SIPC Act in connection with all reasonable requests made by them. Failure to do so shall constitute conduct inconsistent with high standards of commercial honor and just and equitable principles of trade and shall be subject to appropriate disciplinary sanctions depending on the circumstances of the case.

Sincerely,



Gordon S. Macklin
President

Note: The resolution of the Board of Governors regarding this matter appears on the reverse side of this Notice.

RESOLUTION REQUIRING THE COOPERATION OF MEMBERS
WITH TRUSTEES APPOINTED UNDER THE SIPC ACT

WHEREAS, the Association has been advised by the Securities Investor Protection Corporation that certain broker-dealer members of the Association have not been cooperative with trustees of firms for which such has been appointed, pursuant to the Securities Investor Protection Act, where such is required because of outstanding fails, contractual commitments or other matters;

RESOLVED, that all members are hereby directed to cooperate fully with all trustees appointed under the SIPC Act in connection with all reasonable requests made by them. Failure to do so shall constitute conduct inconsistent with high standards of commercial honor and just and equitable principles of trade.

NASD

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

September 19, 1973

TO: NASD Members and Branch Offices
FROM: Gordon S. Macklin, President
RE: New National List Criteria

In a notice dated July 13, 1973, I advised you that the Association was considering certain modifications to the National List criteria. The basic thrust of the proposals was to change the ranking criterion for inclusion in the list from one based primarily on the weighted average weekly volume to one which would rank the issues by dollar value of volume.

The great majority of many thoughtful and constructive comments received were in full agreement with the dollar value approach. However, in response to many additional suggestions from NASDAQ companies, NASD members, and further study by the Association staff, some additional changes to the July 13 proposals were adopted by the Board of Governors on August 24, 1973. A summary of the final requirements follows, and a complete copy of the actual rules is enclosed for your reference.

Based on a ranking made August 24, the National List will be composed of the 2,350 NASDAQ issues which have the highest dollar value of average weekly volume (i.e., the product of their average weekly volume multiplied by the representative bid quotation at the time of compilation of the list), and which meet certain other requirements enumerated later. The changeover will be effective with the publication of markets for October 1, 1973.

As before, the list will be split into two sections. However, the recommended titles have been changed to more clearly reflect the nature and composition of the sections. The 1,400 highest-ranking issues (formerly called the "Most Active National List") will be called the "National OTC-NASDAQ List", and the next 950 issues in the dollar value ranking (previously the "Supplementary National List") will be termed the "Additional OTC-NASDAQ List".

The July 13 proposals contained a provision which would have imposed a minimum average weekly volume standard for qualifying of 1,000 shares for the "Most Active", and 500 shares for the "Supplementary". Our studies, and some of the comments agreed that in view of present market conditions, these cut-off levels were too high.

Therefore, the NASDAQ Committee recommended, and the Board approved, a minimum average weekly volume level of 750 shares for inclusion in the National OTC-NASDAQ List, and no minimum level for qualifying for the Additional List. These standards may need further adjustment at future revision points depending on current market conditions.

The price requirements will remain unchanged from the present standards. Thus, a representative bid quotation of \$5.00 is required for initial authorization for the lists, and a representative bid of \$2.00 at the time the lists are revised is necessary for continuation in either section.

Two final points in the July 13 letter were also approved as proposed. First, both lists will be revised in the future at approximately six-month intervals, instead of the current practice of restructuring the National List every six months and the Additional List every two months. Due to the special restructuring in October, however, we do not anticipate another revision in January 1974 as the regular revision schedule would call for.

Second, in view of the lengthening of the revision date for the Additional List, the NASDAQ Committee in July approved a procedural policy whereby transfers may be made during the interim period between restructuring dates. Under this policy, vacancies which occur in the National OTC-NASDAQ List are filled by the qualified top-ranking issues from either the Additional OTC-NASDAQ List, or issues not currently on either list. Thus, all issues not in the 1,400 list are considered on an equal basis and the top-ranked issues are moved into this list in the order of their ranking. Only issues not on either list are added to the Additional List; i.e., interim transfers from the National OTC-NASDAQ List to the Additional OTC-NASDAQ List are not made. Finally, issues will not be dropped from either list on an interim basis unless they are deleted from the NASDAQ System for any reason, or unless there are fewer than two market makers registered in the System.

A number of additional comments received indicated a strong desire on the part of issuers to be periodically apprised of their rank. In response to these suggestions, a coding system has been developed which will keep issuers more fully informed as to each security's status.

In closing, I would like to emphasize that the NASD furnishes the entire NASDAQ quotations list to various newswire distributors and quotation services. These organizations in turn furnish subscribing publications with whatever data they request. It is the newspapers themselves, then, who determine the amount of space allotted to OTC quotations. We know you want the greatest exposure possible and we assure you that we shall continue our efforts to expand the coverage of over-the-counter markets and NASDAQ securities.

Should you have any questions, please contact David B. Bowman of this office at (202) 833-4899.

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D. C. 20006

NOTICE

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

Date: September 21, 1973

Re: Adoption of New Section 31 of Article III of the Rules of Fair Practice and Appendix B thereunder Concerning Restrictions on Securities "Failed to Receive" and "Failed to Deliver."

Enclosed herewith is a new Section 31 of Article III of the Rules of Fair Practice and Appendix B thereunder which have been declared effective as of September 24, 1973. The new rule was approved by the membership and submitted to and not disapproved by the Securities and Exchange Commission.

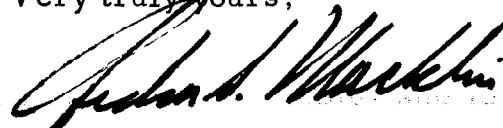
The new Section 31 gives the Board of Governors authority to establish rules, regulations and procedures to be followed by members in connection with domestic and foreign securities which are "failed to receive" and "failed to deliver". Such rules, regulations and procedures are incorporated into Appendix B which the Board of Governors may alter, amend, supplement or modify without recourse to the membership for approval. Any changes in the Appendix, however, must be submitted to and not disapproved by the Securities and Exchange Commission before becoming effective.

Paragraph (a) of the Appendix provides that no member or person associated with a member may sell a security for his own account or buy a security as a broker for a customer (except exempt securities) if

he has a fail to deliver in that security 60 days old or older with respect to domestic securities and 90 days old or older with respect to foreign securities (except American Depository Receipts and Canadian Securities).

Paragraph (b) of the Appendix allows members to request exemptions from the rule for good cause shown and in exceptional circumstances.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Gordon S. Macklin".

Gordon S. Macklin
President

New Material indicated by underlining
Deleted Material indicated by striking out

ARTICLE III, SECTION 31

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 to Article III, Section 31

(a) No member, or person associated with a member, shall sell a security for his own account, or buy a security as a broker for a customer (except exempt securities), if,

- (1) in respect to domestic securities, he has a fail to deliver in that security 60 days old or older; or
- (2) in respect to foreign securities, he has a fail to deliver in that security 90 days old or older (except American Depository Receipts and Canadian securities, which shall be subject to the provisions of paragraph (1)).

(b) For good cause shown and in exceptional circumstances, a member may request exemption from the provisions of this rule by written request to the District Director of the District in which his principal office is located.



NATIONAL CLEARING CORPORATION

UNIFORM PRACTICE DIVISION *

TO: All NASD Members

Transactions made on Monday, October 8, 1973, the day on which Columbus Day will be observed and Monday, October 22, 1973, when Veteran's Day will be observed, and transactions on the business days immediately preceding such days will be subject to the schedule of settlement dates below (for "regular-way" transactions). No settlements will be made on October 8 and October 22, but securities markets and the NASDAQ system will be in operation for trading.

Deliveries of securities and payments of funds ordinarily due on October 8 and October 22, shall be due on the next business day after such dates.

Transactions made on October 8 and October 22 will be combined for settlement with transactions made on the business day preceding such days.

The two days shall not be considered business days in determining the day for settlement of a transaction, the day on which stock shall be quoted ex-dividend, or in computing interest on bonds.

Further, marks to the market, reclamations, buy-ins and sell-outs as provided for in the Uniform Practice Code, shall not be exercised on October 8 and October 22.

Settlement dates for "regular-way" transactions

<u>Trade Date</u>	<u>Settlement Date</u>
October 1	October 9
2	10
3	11
4	12
October 5 and 8	15
15	23
16	24
17	25
18	26
October 19 and 22	29

- Continued -

NATIONAL CLEARING CORPORATION

UNIFORM PRACTICE DIVISION

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Questions regarding this notice may be directed to the Uniform Practice Division of National Clearing Corporation, Two Broadway, 8th Floor, New York, New York, 10004, (212) 952-4018.

- * The Board of Directors of National Clearing Corporation has been delegated the authority to interpret and enforce the provisions of the Uniform Practice Code pending full implementation of NCC's national clearing system.