Issuer Directed Securities

This Interpretation shall apply to securities which are part of a public offering notwithstanding that some or all of those securities are specifically directed by the issuer to accounts which are included within the scope of paragraphs (3) through (8) above. Therefore, if a person within the scope of those paragraphs to whom securities were directed did not have an investment history with the member or registered representative from whom they were to be purchased, the member would not be permitted to sell him such securities. Also, the "disproportionate" and "insubstantial" tests would apply as in all other situations. Thus, the directing of a substantial number of securities to any one person would be prohibited as would the directing of securities to such accounts in amounts which would be disproportionate as compared to sales to members of the public. This Interpretation shall also apply to securities which are part of a public offering notwithstanding that some of those securities are specifically directed by the issuer on a non-underwritten basis. In such cases, the managing underwriter of the offering shall be responsible for insuring compliance with this Interpretation in respect to those securities.

Notwithstanding the above, it may be permissible to sell issuer directed securities to restricted accounts without investment history after first having received permission from the Board of Governors. Permission will only be given where there is a demonstration of valid business reasons for those sales (such as sales to distributors and suppliers or key employees--where such persons are incidentally restricted persons), and the amount of securities directed to such accounts is not substantial or disproportionate as compared to the amount offered to the investing public. Permission will not

be given in situations where the effect would be inconsistent with the obligation to effect a bona fide public distribution.

Investment Partnerships and Corporations

A member may not sell securities of a public offering which immediately after the distribution process is commenced, trade at a premium in the secondary market ("hot issue"), to the account of any investment partnership or corporation, domestic or foreign, (except companies registered under the Investment Company Act of 1940) including but not limited to, hedge funds, investment clubs, and other like accounts unless the member receives from such account, prior to the execution of the transaction, the names and business connections of all persons having any beneficial interest in the account, and if such information discloses that any person enumerated in paragraphs (1) through (4) hereof has a beneficial interest in such account, any sale of securities to such account must be consistent with the provisons of this Interpretation; provided, however, that if the disclosure of such information by the account is prohibited by law, then in such case, the member must receive written assurance from the account that no person enumerated in paragraphs (1) through (4) hereof has a beneficial interest in such account. Such beneficial interest covers not only ownership interests, but every type of financial interest including, but not limited to, management fees based on the performance of the account.

Violations by Recipient

In those cases where a member or person associated with a member has been the recipient of securities of a public offering to the extent that such violated the Interpretation, the member or person associated with a member shall be deemed to be in violation of Article III, Section 1 of the Rules of Fair Practice and this Interpretation as well as the member who sold the securities since their responsibility in relation to the public distribution is equally as great as that of the member selling them. In those cases where a member or a person associated with a member has caused, directly or indirectly, the distribution of securities to a person falling within the restrictive provisions of this Interpretation the member or person associated with a member ~~he~~ shall also be deemed to be in violation of Article III, Section 1 of the Rules of Fair Practice and this Interpretation. Receipt by a member or a person associated with a member of securities of a "hot issue" which is being distributed by an issuer itself without the assistance of an underwriter and/or selling group is also intended to be the subject of the provisions of this Interpretation.

Violations by Registered Representative Executing Transaction

The obligation which members have to make a bona fide public distribution at the public offeing price of securities of a public offering which immediately after the distribution process is commenced trade at a premium in the secondary market ("hot issue"), as stated above, is also an obligation of every person associated with a member who causes a transaction to be executed. Therefore, where sales are made by such persons in a manner

inconsistent with the provisions of this Interpretation, such persons associated with a member will be considered equally culpable with the member for the violations found taking into consideration the facts and circumstances of the particular case under consideration.

Disclosure

The fact that a disclosure is made in the prospectus or offering circular that a sale of securities would be made in a manner inconsistent with this Interpretation does not take the matter out of its scope. In sum, therefore, disclosure does not affect the proscriptions of this Interpretation.

Explanation of Terms

The following explanation of terms is provided for the assistance of members. Other words which are defined in the By-Laws and Rules of Fair Practice shall, unless the context otherwise requires, have the meaning as defined therein.

Public Offering

The term public offering shall mean all distributions of securities whether underwritten or not; whether registered, unregistered or exempt from registration under the Securities Act of 1933, and whether they are primary or secondary distributions, including intrastate distributions and Regulation A

issues, which sell at an immediate premium, in the secondary market. It shall not mean exempted securities as defined in Section 3(a)(12) of the Securities Exchange Act of 1934.

Immediate Family

The term immediate family shall include parents, mother-in-law or father-in-law, husband or wife, brother or sister, brother-in-law or sister-in-law, son-in-law or daughter-in-law, and children. In addition, the term shall also include any other person ~~relative~~ to whose support the member, person associated with the member, or other person in categories (2), (3) or (4) above, contribute directly or indirectly.

Normal Investment Practice

Normal investment practice shall mean the history of investment in an account maintained with the member making the allocation. In cases where an account was previously maintained with another member, but serviced by the same registered representative as the one currently servicing the account for the member making the allocation, such earlier investment activity may be included in the account's investment history. Usually the previous one-year period of securities activity is the basis for determining the adequacy of an account's investment history. Where warranted, however, a longer or shorter period may be reviewed. It is the responsibility of the registered representative effecting the allocation, as well as the member, to demonstrate that the account's investment history justified the allocation of hot issues. Copies of customer account statements or other records maintained by

the registered representative may be utilized to demonstrate prior investment activity. In analyzing an account's investment history the Association believes the following factors should be considered:

1) The frequency of transactions during that period of time. Relevant in this respect are the nature and size of investments.

2) A comparison of the dollar amount of previous transactions with the dollar amount of the hot issue purchase. Obviously, if a restricted person purchases $1,000 of a hot issue and his account revealed a series of purchases and sales in $100 amounts, the $1,000 purchase would not be consistent with the normal investment practice of the account.

3) The practice of purchasing mainly hot issues would not constitute a normal investment practice. The Association does, however, consider as contributing to the establishment of a normal investment practice, the purchase of new issues which are not hot issues as well as secondary market transactions.

Disproportionate

In respect to the determination of what constitutes a disproportionate allocation, the Association uses as a guideline 10% of the member's participation in the issue, however acquired. Thus, if 10% or more of the member's participation in the aggregate is distributed to accounts restricted by the Interpretation, a disproportionate allocation could be considered to have been made. It should be noted, however, that the 10% factor is merely a guideline and is one of a number of factors which are considered in reaching determinations of violations of the Interpretation on the basis of disproportionate allocation. These other factors include, among

other things:

the size of the participation;

the offering price of the issue;

the amount of securities sold to restricted accounts; and,

the price of the securities in the aftermarket.

It should be noted that disciplinary action has been taken against members for violations of the Interpretation where the allocations made to restricted accounts were less than 10% of the member's participation. The 10% guideline is applied as to the aggregate of the allocations.

Notwithstanding the above, a normal unit of trading (100 shares or 10 bonds) will in most cases not be considered a disproportionate allocation notwithstanding the amount of the member's participation. This means that if the aggregate number of shares of a member's participation which is allocated to restricted accounts does not exceed a normal unit of trading, such allocation will in most cases, not be considered disproportionate. For example, if a member receives 500 shares of a hot issue, he may allocate 100 shares to a restricted account or accounts even though such allocation represents 20% of that member's participation. Of course, all of the remaining shares would have to be allocated to unrestricted accounts and all other provisions of the Interpretation would have to be satisfied. Specifically, the allocation would have to be consistent with the normal investment practice of the account to which it was allocated and the member would not be permitted to sell to restricted persons who were totally prohibited from receiving hot issues.

Insubstantiality

This requirement is separate and distinct from the requirements relating to disproportionate allocation and normal investment practice. In addition, this term applies both to the aggregate of the securities sold to restricted acounts and to each individual allocation. In other words, there could be a substantial allocation to an individual account in violation of the Interpretation and yet be no violation on that ground as to the total number of shares allocated to all accounts. The determination of whether an allocation to a restricted account or accounts is substantial is based upon, among other things, the number of shares allocated and/or the dollar amount of the purchase.

~~Definitions~~

~~Where possible, the terms in any interpretation should be defined specifically, but it would be unwise and impractical to attempt to define every word in an interpretation which is based upon business ethics. However, the terms "public offering,"~~ and ~~"immediate family" and "normal investment practice" shall have the meaning for purposes of this Interpretation as stated hereafter. Other words which are defined in the By-Laws and Rules of Fair Practice shall, unless the context otherwise requires, have the meaning as defined therein.~~

Public Offering

The term public offering shall mean all distributions of securities whether underwritten or not; whether registered, unregistered or exempt from registration under the Securities Act of 1933, and whether they are primary or secondary distributions, including intrastate distributions and Regulation A issues, which sell at an immediate premium, in the secondary market. It shall not mean exempted securities as defined in Section 3(a)(12) of the Securities Exchange Act of 1934.

Immediate Family

The term immediate family shall include parents, mother-in-law or father-in-law, husband or wife, brother or sister, brother-in-law or sister-in-law, children and or any other relative to whose support the member, person associated with the member, or other person in categories (2), (3) or (4) above contributes directly or indirectly.

Normal Investment Practice

"Normal investment practice" shall mean the history of investment in an account with the member. Such history must include purchases with some regularity. If such history discloses a practice of purchasing mainly "hot issues" such record would not constitute a "normal investment practice" as used in this Interpretation.

[Interpretation adopted effective November 1, 1970; amended effective January 11, 1972, March 12, 1972 and December 1, 1973.]

NOTICE TO MEMBERS: 82-18
Notice to Members should be retained for future reference.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
1735 K STREET NORTHWEST · WASHINGTON, D.C. 20006 · (202) 833-7200

March 24, 1982

TO: All NASD Members and Municipal Securities Bank Dealers

ATTN: All Operations Personnel

RE: Holiday Settlement Schedule

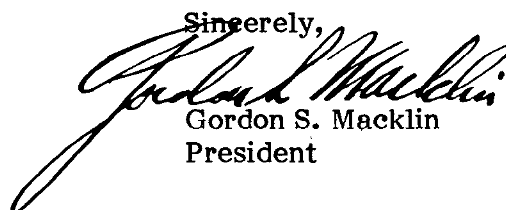
Securities markets and the NASDAQ System will be closed on Good Friday, April 9, 1982. "Regular-Way" transactions made on the business days immediately preceding that day will be subject to the following schedule.

Trade Date-Settlement Date Schedule
For "Regular-Way" Transactions

Trade Date	Settlement Date	*Regulation T Date
April 2	April 12	April 14
5	13	15
6	14	16
7	15	19
8	16	20
9	Good Friday	—
12	19	21

The foregoing settlement dates should be used by brokers, dealers and municipal securities dealers for purposes of clearing and settling transactions pursuant to the Association's Uniform Practice Code and Municipal Securities Rulemaking Board Rule G-12 on Uniform Practice. Questions concerning the application of these settlement dates to a particular situation should be directed to the Uniform Practice Department of the NASD at (212) 938-1177.

Sincerely,



Gordon S. Macklin
President

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* Pursuant to Section 4(c)(2) of Regulation T of the Federal Reserve Board, a broker-dealer must promptly cancel or otherwise liquidate a purchase transaction in a cash account if full payment is not received within seven (7) business days of the date of purchase or, pursuant to Section 4(c)(6), make application to extend the time period specified. The date members must take such action is shown in the column entitled "Regulation T Date".

Notice to Members 82-19
Notices to members should be retained for future reference.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
1735 K STREET NORTHWEST · WASHINGTON, D.C. 20006 · (202) 833-7200

March 26, 1982

TO: All NASD Members and Other Interested Persons

RE: Proposed Amendments to SEC Rule 10b-6

The Securities and Exchange Commission recently proposed amendments significantly liberalizing Rule 10b-6 under the Securities Exchange Act of 1934. Rule 10b-6 restricts bids and purchases by market-makers, other broker/dealers, and issuers prior to a distribution of securities. The rule presently requires that market-makers withdraw from the market at least ten days prior to the effective date of an offering in which they intend to participate.

The proposed amendments, some of which may be relied upon immediately, would permit market-makers and other participants in a distribution to continue trading until three days before the commencement of the distribution, would narrow the scope of the rule through a definition of the term "distribution," and would codify existing SEC staff positions concerning certain exceptions to the rule. The proposed amendments are discussed below.

The Commission is soliciting comments on the amendments until April 30, 1982. The amendments are described in Securities Act Release No. 6387 (March 3, 1982), copies of which are available from the Association's Corporate Financing Department.

Background

The proposed amendments are the first major revisions of Rule 10b-6 since it was adopted in 1955. The rule is intended to prevent participants in a distribution of securities from engaging in manipulative activities designed to create a false impression of market activity that would facilitate the sale of the securities at artificially high prices. The rule prohibits persons connected with a distribution from bidding for or purchasing the securities being distributed, as well as other securities which may affect the market, prior to and during the distribution. The general prohibition is subject to exceptions for certain transactions.

Without changes to the rule to reflect changes in the securities markets, the rule's requirements have become increasingly burdensome over the past several years. The Association has been concerned about the impact of the rule, particularly on NASDAQ market-makers and issuers. Last year the Board of Governors established an Ad Hoc Committee on SEC Rule 10b-6 which developed a detailed proposal for amending the rule. That proposal was submitted to the SEC in November. Several of the proposed amendments parallel those sought by the Association.

Summary of Commission Proposals

A summary of the proposed amendments to Rule 10b-6 and other actions taken by the Commission and staff follows.

Exception (xi) - The Commission is proposing to amend Exception (xi) to section (a)(2) of the rule to reduce the period preceding an offering during which a broker/dealer participating in the offering must refrain from purchasing the security being offered. For solicited transactions, the restriction period would begin on the third business day prior to the proposed commencement of the distribution or at the time a broker/dealer becomes a participant in the distribution, whichever is later. Therefore, if a member of the underwriting or selling group, other than the managing underwriter, receives an invitation to participate in the offering within three business days prior to the proposed commencement, Rule 10b-6 is satisfied if solicited bids and purchases cease at that point. Unsolicited transactions would be permitted until the distribution commences. The rule presently requires broker/dealers to refrain from solicited transactions for ten business days and unsolicited for five days.

In addition, the Commission is proposing that Exception (xi) be available not only in the over-the-counter market, but for exchange transactions as well.

The Commission staff is taking an interim "no action" position (until the Commission takes final action on the Rule 10b-6 proposals) with reference to persons who comply with the proposed amendments to Exception (xi) where the issuer is qualified to register on new Forms S-2 or S-3* under the Securities Act of 1933 ("1933 Act"). Forms S-2 and S-3 require that the issuer have been a reporting company for at least three years. This interim "no action" position also applies to shelf registra-

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* Forms S-1, S-2 and S-3 and temporary Rule 415(T) relating to shelf registrations were adopted by the Commission as part of the integrated disclosure system at the same time that the amendments to Rule 10b-6 were proposed. See Securities Act Release No. 6383 (March 3, 1982).

tions pursuant to new temporary Rule 415(T) under the 1933 Act. Until final action on the Rule 10b-6 proposals, therefore, market-makers who participate in an offering on an S-1 registration statement must comply with the ten-day "cooling-off" period.

The Commission is specifically requesting comments as to whether a "cooling-off" period of more than three days is necessary for distributions of certain securities, such as securities of an issuer only qualified to use Form S-1.

In its submission to the Commission, the Association sought clarification of permissible market activity during the three-day "cooling-off" period. The Commission has indicated that pre-effective stabilization may be made pursuant to Rule 10b-7(e) under certain circumstances. The Commission is requesting comments as to whether Rule 10b-6 should be amended to permit limited market-making activity during the three-day period.

Definition of "Distribution" - The Commission has proposed a definition intended to clarify those transactions which constitute a "distribution" for purposes of Rule 10b-6. The definition distinguishes a distribution from ordinary trading transactions by reference to the magnitude of the offering or the presence of special selling efforts or the payment of increased compensation.

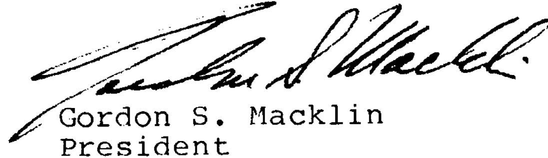
The proposed definition also includes a codification of the SEC staff interpretation that sales of securities in compliance with the "volume" and "manner of sale" provisions of Rule 144 under the 1933 Act is not considered a Rule 10b-6 distribution thus providing a "safe harbor."

Exception (xii) - The Commission is proposing a new exception to relax the application of the rule to issuers of securities. Exception (xii) would permit issuers, selling shareholders and their affiliated purchasers to continue to purchase all outstanding securities of the issuer until three business days prior to any sales of the securities to be distributed. Unlike Exception (xi), however, during the three-day period both solicited and unsolicited transactions are prohibited.

The Commission staff is taking an interim "no action" position with reference to shelf offerings, which are considered to be Rule 10b-6 distributions, made in accordance with temporary Rule 415(T) if issuers, selling shareholders and their affiliated purchasers comply with proposed Exception (xii), provided the issuer qualifies to use new registration Forms S-2 or S-3. The staff will not, however, take a similar "no action" position with reference to offerings which are not made pursuant to Rule 415(T).

Any questions regarding this Notice may be directed to Dennis C. Hensley or Suzanne E. Rothwell of the Corporate Financing Department at (202) 833-7240.

Sincerely,



Gordon S. Macklin
President

Exception (xiii) - The Commission is proposing new Exception (xiii) to allow purchases of certain investment grade debt securities of the issuer during a distribution of similar debt securities if certain conditions are met. The conditions relate to the reporting requirements of the issuer, the amount of the issuer's outstanding public debt and the ratings of the debt securities involved.

The Commission is taking an interim "no action" position with reference to shelf offerings of debt securities pursuant to temporary Rule 415(T), if all the conditions of proposed Exception (xiii) are met until final Commission action on the Rule 10b-6 proposals. In addition, where the conditions of Exception (xiii) cannot be met, the Commission is proposing to take a "no action" position where the outstanding debt security purchased varies by at least one percent in the coupon interest rate and by at least ten years in the maturity date from those of the debt securities being distributed.

Miscellaneous - The Commission is proposing to amend a number of other exceptions to Rule 10b-6 to clarify their application. In addition, the Commission is proposing to amend the rule to clarify that an underwriter is not considered to have completed its participation in a distribution until any over-allotment option has been either exercised or cancelled. The Commission is also excepting from Rule 10b-6 purchases made in accordance with Rule 10b-8 by underwriters of convertible securities pursuant to a standby agreement in connection with a redemption call for the securities by the issuer.

* * * *

The Association expects to comment favorably on the proposed liberalization of Rule 10b-6, particularly the newly-reduced three-day "cooling off" period before offerings. There is serious concern, however, over the Commission's proposal to require a longer period for less-seasoned companies (those using Form S-1). Members who wish to submit comments to the Commission on these proposals should refer to SEC File No. S7-921 and address their comments to George A. Fitzsimmons, Secretary, Securities and Exchange Commission, 500 North Capitol Street, Washington, D.C. 20549.

Proposed Changes
to
SEC Rule 10b-6

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 33-6387; 34-18528; IC-12266; File No. S7-921]

Prohibitions Against Trading by Persons Interested in a Distribution

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rulemaking.

SUMMARY: The Commission is proposing for comment amendments to Rule 10b-6 under the Securities Exchange Act of 1934 ("Act") that regulates trading in securities by persons who are participating in a distribution of those

securities. If adopted, the amendments, among other things, would define the term "distribution" for purposes of that rule, permit participants in a distribution of securities to continue trading such securities until three business days before commencement of the sales of the securities being distributed, and clarify the applicabilty of the rule to persons who participate in a delayed offering of securities by the issuer. In addition, the amendments would codify several existing staff positions under the rule with respect to the applicability of the exceptions to the rule. The Commission also is publishing for comment an amendment to Rule 10b-8 under the Act which applies to purchases during rights offerings. The amendment will extend the scope of the rule to cover purchasing activity by broker-dealers who act as "standby underwriters" in connection with a call for redemption by an issuer of its convertible securities. Finally, the Commission is proposing for comment certain technical conforming amendments to Rule 10b-8 and to Rule 10a-1 under the Act which governs short sales.

DATE: Comments should be submitted on or before April 30, 1982.

ADDRESSES: Interested persons should submit six copies of their written data, views and arguments to George A. Fitzsimmons, Secretary, Securities and Exchange Commission, Room 892, 500 North Capitol Street, Washington, D.C., 20549, and should refer to File No. S7-921. All submissions will be available for public inspection at the Commission's Public Reference Section, Room 6101, 1100 L Street NW., Washington, D.C.

FOR FURTHER INFORMATION CONTACT: Any of the following attorneys in the Office of Legal Policy and Trading Practices, Division of Market Regulation, Securities and Exchange Commission, 500 North Capitol Street, Washington, D.C., 20549: John B. Manning, Jr. (202-272-2874); Mary Chamberlin (202-272-2880); M. Blair Corkran, Jr. (202-272-2853); Kenneth B. Orenbach (202-272-2871); Carlos M. Morales (202-272-2876); Joel M. Bludman (202-272-2846); Allyn C. Shepard (202-272-2878); Eric E. Miller (202-272-2882); or Eneida Rosa (202-272-2828).

SUPPLEMENTARY INFORMATION:

Introduction

The Securities and Exchange Commission is publishing for comment amendments to Rule 10b-6 (§ 240.10-6) under the Act. If adopted, these amendments generally would define the term "distribution" for purposes of rule, relax the prohibitions of the rule and codify existing staff positions concerning some of the exceptions to the rule. In addition, the Commission is publishing for comment a related amendment to Rule 10b-8 (§ 240.10b-8) under the Act which applies to purchases during rights offerings. The amendment will extend the scope of the rule to cover purchasing activity by broker-dealers who act as "standby underwriters" in connection with a call for redemption by an issuer of its convertible securities.

Rule 10b-6 is an anti-manipulative rule that, subject to certain exceptions, prohibits persons who are engaged in a distribution of securities from bidding for or purchasing, or inducing other persons to bid for or purchase, such securities, any security of the same class and series as those securities, or any right to purchase any such security until they have completed their participation in the distribution. The purpose of the rule is to prevent participants in a distribution from artificially conditioning the market for the securities in order to facilitate the distribution. The rule is designed to protect the integrity of the auction market as an independent pricing mechanism and thereby enhance investor confidence in the marketplace. The rule contains eleven exceptions to its general prohibitions that are designed to facilitate an orderly distribution of securities or limit disruption in the trading market for the securities being distributed.

Rule 10b-6 was adopted together with Rules 10b-7 (§ 240.10b-7) and 10b-8 in 1955[1] after years of Commission and industry experience under the antifraud and anti-manipulative provisions of the federal securities laws. In large measure, the rules codified principles established in prior administrative interpretations and proceedings concerning trading activity in connection with distributions.[2] Rule 10b-6 has been, and continues to be, one of the most important means of ensuring that the marketplace is free of manipulative practices.

Nevertheless, since 1955, the structure and operation of the securities markets have changed dramatically. The dissemination of market information with respect to securities transactions has been vastly improved. Also since that time, the techniques that have been developed to effect distributions of securities, including public offerings an in connection with business combinations, have become increasingly complex while the entire process by which securities are registered for sale has been streamlined.

Many of these developments have raised questions under Rule 10b-6 that were not contemplated when the rule was adopted, or have involved transactions that would be prohibited if the rule were literally applied but which do not present a significant opportunity for manipulative abuse. Through the exemptive and no-action interpretive process, the Commission and its staff have attempted to accommodate the rule to changing business needs to the extent consistent with its anti-manipulative purpose. A result of this process, however, has been the development of staff positions concerning the interpretation of the rule in the context of various kinds of transactions which have required application to the Commission for exemptive relief, or which have not received adequate publicity and therefore have created a degree of uncertainty among members of the securities community. The Commission believes that the amendments will eliminate much of this uncertainty and substantially reduce the need to seek interpretive relief under the rule.

The changes in the markets since the rule was adopted also have raised the more fundamental question of whether the general prohibitions of the rule are more restrictive than necessary to accomplish its purposes. Under existing standards of the rule, for example, broker-dealers that participate in an underwritten public offering on behalf of an issuer whose securities are traded exclusively on a national securities exchange are often prohibited from making any market purchases of those securities that are not specifically excepted by the rule for a substantial period before the registration statement is declared effective. In many cases, this period may be longer than is necessary to dissipate the market effect of purchases by those broker-dealers. In addition, although the rule permits certain participants in a distribution of securities that are traded in the over-the-counter market to continue market-making activity in those securities until ten business days before the commencement of the distribution, it has been argued that the length of the "cooling-off" period has resulted in a significant decrease in liquidity in the market for those securities and adversely affected the pricing of the

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[1] Securities Exchange Act Release No. 5194 (July 5, 1955). *See also* Securities Exchange Act Release Nos. 5040 (May 18, 1954) (publishing proposals for comment), and 5159 (April 19, 1955) (publishing revised proposals for comment).

[2] *See, e.g.,* Securities Exchange Act Release Nos. 3505 and 3506 (November 16, 1943).

offered securities.[3] In this regard, the National Association of Securities Dealers ("NASD") has submitted a letter, dated November 19, 1981, discussing this problem and related concerns under the rule, and has suggested revisions to the rule.[4]

The application of Rule 10b-6 has also raised special concerns in the context of Rule 415 under the Securities Act of 1933 ("Securities Act") which now permits, on a temporary basis, additional kinds of "shelf" offerings by issuers.[5] Among the issues raised are the manner in which the term "distribution" should be interpreted in the context of these kinds of offerings, and the applicability of the rule generally to persons who participate in such offerings. The Commission solicited comment on these and other market-related issues in the two releases proposing Rule 415, then denominated as Rule 462A, for comment.[6]

In light of all of these concerns, the Commission has re-examined Rule 10b-6 and is publishing for comment comprehensive amendments to the rule. These proposals not only would codify existing staff interpretations of the rule, but also would significantly relax the prohibitions of the rule generally in a manner that the Commission believes shoulf continue to preserve the integrity of the marketplace. If the proposals are adopted, the rule would permit underwriters and prospective underwriters to continue purchasing activity until three business days before commencement of any offers or sales in a distribution. The rule would not distinguish between distributions of securities traded in the over-the-counter market and those traded on an exchange. In addition, the rule would permit issuers and certain related persons to make purchases of the issuer's stock that is the subject of a distribution until three business days before commencement of any offers or sales in the distribution. The amendments also would clarify the applicability of the rule to persons who participate in "shelf" offerings under new Rule 415.

The Commission also is proposing to define the term "distribution" for purposes of the rule. The definition would codify the principles established through administrative and judicial decisions, and would provide that sales of securities that are made in compliance with the volume and manner of sale limitations of Rule 144 (§ 230.144) under the Securities Act will not constitute distributions for purposes of Rule 10b-6.

The discussion concerning the proposed amendments to Rule 10b-6 is divided into three parts. The first discusses the proposed definition of the term "distribution" for purposes of the rule, including the Commission's views on the manner in which that term would be interpreted in the context of shelf offerings under Rule 415. The second part discusses the relaxation of the rule's prohibitions generally by amendment to Exception (xi) and proposed Exception (xii) which would be available to issuers and other persons. A specific discussion has been included concerning the operation of these exceptions in an offering conducted under Rule 415. The third part of the discussion details the proposed amendments to exceptions (ii), (iii), (iv) and (vii) of the rule (and certain conforming changes to Rule 10a-1 (§ 240.10a-1) under the Act and Rule 10b-8), proposed new exceptions that relate to purchases of certain debt securities, the status of "overallotment" options for purposes of the rule, and the proposed amendment to Rule 10b-8 in connection with standby underwriting arrangements.

I. The Term "Distribution" for Purposes of Rule 10b-6

A. Proposed Definition

Rule 10b-6 does not expressly define the term "distribution." Nevertheless, judicial and administrative cases consistently have held that the primary indicia of a distribution for purposes of the rule are the magnitude of the offering or the types of selling efforts and selling methods utilized by the seller or its agents.[7] While employing these factors to determine the existence of a distribution, the Commission historically has declined to adopt an explicit definition of the term, preferring instead to determine on a case-by-case basis whether a particular transaction or series of transactions constitutes a distribution for purposes of Rule 10b-6.[8] The primary advantage of such an *ad hoc* approach has been the flexibility it provides for the courts and the Commission to apply the rule to a large and continually evolving variety of transactions that may give rise to manipulative potential. On the other hand, this approach has resulted in a lack of certainty for persons engaged in the securities business as to the parameters of the concept of distribution for purposes of the rule.

The Commission has reconsidered its traditional position and is now proposing a definition of the term distribution in order to provide guidance to the investment community concerning the scope of Rule 10b-6.[9] The NASD, in connection with its proposed revisions to various portions of Rule 10b-6, has also suggested a definition of distribution.[10] The Commission shares the NASD's concern that persons potentially subject to the prohibitions of Rule 10b-6 should be provided added assistance in determining whether their activities constitute a distribution within the meaning of the rule. Indeed, substantial benefits may be realized from an added degree of predictability concerning the types of activities that are contemplated by the term.

The Commission's proposed definition would, in broad terms, codify the current case law. The proposed definition distribution for purposes of Rule 10b-6 from ordinary trading transactions and the normal conduct of a securities business by reference to the magnitude of the offering or the presence of special selling efforts or the payment of increased amounts of compensation in connection with the sale of the subject securities.[11] It also would provide that transactions which comply with the volume and manner of sale provisions of Rule 144 under the Securities Act will not be deemed to

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[3] *See* Section II.A., *infra.*

[4] *See* letter dated November 19, 1981 from Frank J. Wilson, Esq., Executive Vice President, NASD, to Douglas Scarff, Director, Division of Market Regulation ("NASD Letter") which is publicly available in File No. S7-921.

[5] *See* Securities Act Release No. 6383, (March 3, 1982), adopting the integrated disclosure proposals. Rule 415 has been adopted for a period of nine months. In June, 1982, the Commission will hold public hearings on issues raised by Rule 415.

[6] *See* Securities Act Release Nos. 6276 (December 23, 1980), 46 FR 78 (1980); 6334 (August 18, 1981) 46 FR 42001 (1981).

[7] *See, e.g., In the Matter of Bruns, Nordeman & Co.*, 40 SEC 652 (1961). These criteria identify offerings of securities that may present an incentive for participants to engage in manipulative purchasing activities.

[8] *See, e.g., In the Matter of Collins Securities Corp.*, Securities Exchange Act Release No. 11766 (Oct. 23, 1975) *rev'd on other grounds, Collins Securities Corp. v. SEC*, 562 F.2d 320 (D.C. Cir. 1977); *In the Matter of F.S. Johns & Co., Inc.*, 43 SEC 124 (1966); *In the Matter of Theodore A. Landau*, 40 SEC 1119 (1962).

[9] Following its review of any comments received with respect to the proposed definition of distribution, the Commission intends to publish a release, in a question and answer format, addressing specific situations and fact patterns that have caused uncertainty in connection with the scope of a distribution within the meaning of Rule 10b-6.

[10] *See* NASD Letter at 6-7.

[11] Payment of increased compensation gives rise to an incentive on the part of an agent acting for the issuer or selling shareholder to engage in special selling efforts, including the solicitation of customer orders to purchase the securities being sold.

constitute distributions for purposes of Rule 10b–6.

The NASD's proposal would define the term distribution as any "public offering" of securities, whether or not subject to registration under the Securities Act, provided that the amount of securities to sold exceeds that permitted by paragraph (e) of Rule 144. Furthermore, the NASD, like the Commission, would distinguish a distribution from ordinary selling activities by requiring the presence of selling efforts or compensation, either of which is greater than that normally found in connection with the ordinary trading activities of market professionals.

A "public offering" is a term that under the Securities Act, has a generally accepted meaning.[12] In a "public offering" the securities to be sold must be offered only pursuant to an effective registration statement. The effective date of a registration statement controls the commencement of a public offering under the Securities Act. For purposes of Rule 10b–6, however, the Commission has consistently taken the position that a distribution of securities to be sold pursuant to a public offering under the Securities Act may commence not only before a registration statement with respect to those securities has become effective, but even before such statement has been filed with the Commission. A distribution commences at the point when the incentive to enage in manipulative conduct is first present. Accordingly, with respect to the issuer, a distribution generally is deemed to commence at the time that a determination to go forward with the public offering is made. An underwriter is deemed to be a participant in a distribution from the time it reaches an agreement with the issuer with respect to a future public offering. In addition, the Commission has held that a distribution for purposes of Rule 10b–6 is not limited to a "public offering under the Securities Act.[13] This position recognizes the fact that the potentially manipulative market effects that Rule 10b–6 was designed to prevent may occur in connection with non-public offerings that are distinguishable from ordinary trading transactions.[14] These long-standing interpretations under Rule 10B–6 make it evident that a distribution and a public offering are not synonymous for purposes of the rule.[15]

The Commission also is not inclined to adopt a *per se* volume test in order to determine the existence of a distribution for purposes of Rule 10b–6. Concentrating solely on the magnitude of the offering ignores the fact that the sale of an amount of securities that is within the volume limits of Rule 144 may nevertheless, as a result of the selling methods utilized, give rise to a distribution for purposes of Rule 10b–6.[16] The Commission proposes, however, to codify the staff's view that sales of any securities made in compliance with both the volume limitations [17] and the "manner of sale" provisions [18] of Rule 144 will not be deemed to be a distribution for purposes of the Rule 10b–6.

Pursuant to the "manner of sale" provisions of Rule 144, securities must be sold either in brokerage transactions [19] or in transactions directly with a "market maker" within the meaning of the Act.[20] The purpose of these restrictions is to ensure that sales pursuant to Rule 144 will be made only in routine trading transactions and in a manner expressly designed not to disrupt normal market operations. In order to qualify for the protection from liability that Rule 144 provides, a seller is also prohibited from either soliciting orders from prospective purchasers to buy the securities or making any special compensation arrangements in connection with the sale of such securities.[21] A Rule 10b–6 distribution is often evidenced by extraordinary selling methods and efforts to dispose of the securities that are greater than those normally engaged in by market participants in the day-to-day transaction of their business. In view of the conditions imposed by Rule 144 on both the amount of securities that may be sold and the manner in which such sales are required to take place, the Commission believes that it would be difficult to identify a distribution if all such conditions are satisfied.

Commentators are specifically requested to address the question of whether the proposed definition would meet the perceived need for certainty within the context of Rule 10b–6 or whether it would be preferable to retain the current practice of determining the existence of a distribution for purposes of Rule 10b–6 on a case-by-case basis.

B. Application of the Term "Distribution to Shelf-Registered Offerings

The term "distribution" will have special significance in the context of certain of the offerings now permitted by Rule 415 under the Securities Act. That rule permits the registration of securities that are to be offered and sold on a delayed or continuous basis. Among other things, the rule permits an issuer to sell securities registered on a shelf in a succession of different kinds of offerings. It is designed to facilitate capital formation by granting ready access to the trading market. In the releases proposing Rule 462A for comment,[22] the Commission specifically requested comment on how the term distribution should be interpreted in connection with these offerings.

In the Commission's view, the determination of whether a distribution exists for purposes of Rule 10b–6 in the context of a shelf-registered offering should depend on the same factors that indicate an incentive to manipulate in connection with any offering of securities. Accordingly, the definition of distribution proposed above would have the same application in the context of a shelf-registered offering as in the more traditional forms of distributions. Whether a shelf-registration will constitute a distribution for purposes of Rule 10b–6 will depend on factors that include the number of shares that are to be registered for sale by the issuer and the percentage of the outstanding shares, the public float and the trading volume that those shares represent. If the registrant, when disclosing its proposed plan of distribution, reserves the right to utilize techniques that might entail selling efforts or compensation of the type normally associated with a distribution, the entire shelf-registered offering will be deemed to constitute a single distribution for purposes of Rule 10b–6.[23] Applying this analysis, the Commission believes that many shelf-registered offerings will constitute Rule 10b–6 distributions.[24]

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[12] *See, e.g.*, Section 4(2) of the Securities Act and Rules 146, 152 and 155 thereunder.

[13] *See, e.g.*, *In the Matter of J.H. Goddard & Co., Inc.*, Securities Exchange Act Release No. 7618 (June 4, 1965).

[14] *See, e.g.*, *In the Matter of Collins Securities Corp.*, Securities Exchange Act Release No. 11766 (Oct. 23, 1975) at 13–14.

[15] *See id.* at 13.

[16] *See* Securities Act Release Nos. 5979 (Sept. 19, 1978) and 6286 (Feb. 6, 1981) at nn. 7 and 13.

[17] Rule 144(e).

[18] Rule 144(f).

[19] "Brokerage transactions" are described in paragraph (g) of Rule 144.

[20] Section 3(a)(38) of the Act defines "market maker."

[21] Rule 144(f)(1)–(2).

[22] *See* note 6, *supra*.

[23] The same factors will be employed to determine whether a secondary offering of securities registered on the shelf will give rise to a distribution for purposes of Rule 10b–6. For purposes of a Rule 10b–6 distribution, a secondary offering made pursuant to Rule 415 will be treated in the same way as a primary shelf-registered offering.

[24] The commentators that addressed the question of the interpretation of the term "distribution" in the context of shelf-registered offerings suggested that issuers and market professionals should be viewed

Continued

For purposes of shelf-registered offerings, an issuer should be deemed to be engaged in a distribution of its securities from the time it determines to proceed with a shelf-registration of equity securities that meets the criteria of a distribution.[25] The Commission agrees with certain of the commentators on proposed Rule 462A, however, that issuers should not be subject to the strict prohibitions of Rule 10b-6 throughout the life of the shelf. Accordingly, as discussed more fully elsewhere in this release,[26] the Commission is proposing a new exception, analogous to the current Exception (xi), that would reduce the impact of the rule's strict prohibitions on issuers.

A broker-dealer that has a continuing agreement with the registrant to sell the securities registered on a shelf will be deemed to have commenced its participation at the time it reaches such an agreement. Since the arrangement in connection with a shelf-registered offering may last for a substantial length of time, the Commission is also proposing an amendment to Exception (xi) of the rule [27] to permit such broker-dealers to effect bids for or purchases of the securities that are the subject of the distribution until three business days before the commencement of any sale. The rule as revised will continue to apply to other broker-dealers who participate from time to time in the registrant's distribution in much the same way that it does currently. When a broker-dealer accepts an invitation to participate in the sale of securities that are registered on the shelf, the rule's prohibitions would not apply until the later of that time or three business days before commencement of any sales.

II. General Relaxation of Trading Restrictions

A. Exception (xi)

Exception (xi) currently permits underwriters, prospective underwriters and dealers who are participants in a distribution of securities to bid for or purchase the security which is the subject of the distribution until ten business days prior to the proposed commencement of such distribution (or five business days in the case of unsolicited purchases) provided that such bids and purchases are made otherwise than on a securities exchange. At the time of its adoption, this exception was designed to address the special liquidity problems caused by the operation of Rule 10b-6 in markets for unlisted over-the-counter securities during distributions of those securities.[28] When issuers whose securities are traded in the over-the-counter market decide to raise capital by engaging in a public offering of their securities, they typically select broker-dealers that make a market in their securities to act as underwriters. These market makers ordinarily constitute the principal market for the security, are knowledgeable about the security and generally are aware of the extent of investor interest in the security. Without the relief afforded by Exception (xi), however, each of these market makers would generally be prohibited from making a market in the security from the time it decided to accept an invitation to participate in the distribution. As a result, since this time often is far in advance of the actual commencement of selling efforts, the depth and liquidity of the market for the securities could be significantly reduced, which in turn might adversely affect the pricing of the issue.

In view of these significant concerns, the Commission believed at the time Rule 10b-6 was adopted that Exception (xi), in conjunction with the other exceptions to the rule, including Exception (viii), which permits stabilization not in violation of Rule 10b-7, constituted a suitable compromise between the Rule 10b-6 policy that distributions should be carried out free of the influence of any bids and purchases by participants and the need to preserve liquidity in the markets for unlisted over-the-counter securities that are the subject of distributions. At that time, ten business days was believed to be the time needed to ensure the elimination of participant influence.

Since the adoption of Rule 10b-6 in 1955, the securities markets have undergone significant change. In view of these changes and on the basis of the Commission's experience in administering the rule, the Commission now believes that Rule 10b-6 generally and Exception (xi) specifically may be more restrictive than necessary to accomplish the rule's purpose.

The application of Rule 10b-6 has also raised special concerns in the context of new Rule 415 that permits new kinds of "shelf" offerings by issuers and others.[29] Under Rule 10b-6, broker-dealers that have continuing agreements with the issuer to sell from time to time securities that are registered on the shelf would be deemed to be participants from the time they enter into such agreements until the earlier of the termination of the agreement or the completion of the sales which are covered by the agreement.[30] Such broker-dealers would therefore be subject to the prohibitions of Rule 10b-6 for a substantial period of time, and possibly, far in advance of their participation in any sales of the securities registered on the shelf. The restrictions on these broker-dealers for extended periods of time would have an adverse impact on liquidity in the markets for the securities that are the subject of the distribution. In addition, if broker-dealers were so strictly limited, issuers would not be able to take advantage of favorable market conditions in the manner envisioned by new Rule 415 in both the exchange and over-the-counter markets. In response to these problems, several commentators on the releases proposing Rule 462A for comment suggested that Rule 10b-6 be amended to address the problems of broker-dealers who had a continuing agreement with the issuer. Since the problems that are encountered under Rule 10b-6 by broker-dealers that participate in distributions involving a shelf offering are analogous to the problems that are perceived to exist with respect to Exception (xi), the Commission believes that these problems should be addressed at the same time.

In addition, the NASD recently proposed that the Commission replace current Exception (xi) with two new exceptions to Rule 10b-6.[31] The first would permit participants to make a market in the security that is the subject of a distribution until two business days before the commencement of the distribution and would permit such participants to make unsolicited purchases until the commencement of

as being engaged in a series of distributions rather than a single distribution. The underlying concern appeared to be that if the Commission took the single distribution position, it would significantly interfere with purchasing activity in the issuer's securities by participants in the distribution during periods when no sales were being made off the shelf. The commentators agreed with the Commission, however, that under either approach, a short cooling-off period would be appropriate between market purchases and sales off the shelf. This is the approach the Commission has taken in the proposed amendment to Exception (xi) and in proposed Exception (xii). *See* Section II., *infra*.

[25] *See* Section I.A., *supra*.

[26] *See* Section II.B., *supra*.

[27] *See* Section II.A., *supra*.

[28] The provisions of Rule 10b-6 do not give rise to similar liquidity problems in markets for exchange-traded securities. In the exchange markets, specialists continue to maintain markets in securities that become the subject of distributions for purposes of Rule 10b-6 even after the broker-dealers participating in the distributions are required to cease bidding for and purchasing the subject securities.

[29] *See* text & nn. 5-6, *supra*.

[30] *See* Section I.B., *supra*.

[31] *See* NASD Letter at 2-6.

the offering. The other exception would permit participants who are registered as market makers with the inter-dealer quotation system in which they propose to make stabilizing bids and purchases to engage in market-making during the two business days prior to the commencement of a firm commitment offering at a price not in excess of the highest independent bid for such security displayed in that system on the third business day prior to the commencement of the offering.

The Commission is proposing that current Exception (xi) be amended generally to reduce the ten business day cooling-off period to three business days for solicited purchases and to permit unsolicited purchases until the commencement of sales.[32] As amended, Exception (xi) no longer would distinguish between bids and purchases made on an exchange and those made in the over-the-counter market. It would permit bids and purchase of a security in distribution until three business days before the commencement of sales of the security both in the context of shelf-registered distributions contemplated by Rule 415 and in the context of traditional kinds of distributions. These proposed amendments, detailed below, are designed to accommodate the changes in the market that have taken place since the adoption of Rule 10b-6, and to facilitate the use of new techniques for distributing securities.

For several reasons, the Commission is not proposing to amend Rule 10b-6 at this time to permit limited market-making activity during the three day cooling-off period as suggested by the NASD. First, although the use of pre-effective stabilization has not developed in the past, the Commission believes that where the cooling-off period is as short as three days many of the problems previously encountered by syndicate managers contemplating pre-effective stabilization will be remedied.[33] In addition, to the extent that pre-effective stabilization generally becomes more feasible, it will become more practicable for members of syndicates in the over-the-counter market to make multiple stabilizing bids and purchases as permitted by Rule 10b-7(e), provided that the bids and purchases are made on behalf of the syndicate account as required by Rule 10b-7(e). Moreover, the Commission is concerned that to go beyond what is currently permissible under Rule 10b-7 during the very short cooling-off period being proposed today might result in uncoordinated stabilizing by members of the underwriting syndicate for their own account. Such activity might ultimately cause disruption in the capital markets and in fact compromise the independence of the market as a pricing mechanism. Commentators, however, are invited to address this point specifically.

1. *Three day cooling-off period.* The Commission is proposing to amend Exception (xi) to permit underwriters, prospective underwriters or dealers to make bids or purchases of the security being distributed (and the other securities covered by the rule) up until three business days before the commencement of an offering, and to eliminate the current distinction between exchange and over-the-counter transactions for purposes of Exception (xi). Although Exception (xi) was originally prompted by a need to assure continued liquidity in the over-the-counter markets to the extent consistent with the rule's purposes, the Commission believes that the ten day cooling-off period that it imposes is unnecessarily long. In view of the speed with which information is disseminated in today's market place, the Commission believes that a three day cooling-off period, at least with respect to certain securities, generally should be sufficient to dissipate the market impact of a participating broker-dealer's purchases prior to the commencement of sales. Although this amendment would appreciably reduce the cooling-off period, the Commission does not believe that the amendment should sacrifice the integrity of the markets. Together with the general antifraud and anti-manipulative provisions of the federal securities laws, particularly section 9(a)(2) and section 10(b) and Rule 10b-5 thereunder, Rule 10b-6 should continue to provide sufficient investor protection. The Commission has some concern, however, that the potential for manipulative abuse may be greater in the context of distributions of securities conducted on behalf of issuers that are required to use new Form S-1 under the Securities Act of 1933 which the Commission has adopted as part of its integrated disclosure system.[34] The market for these securities may be less stable relative to the markets for securities of issuers that are qualified to use Forms S-2, or S-3. In addition, issuers required to use Form S-1 will not have extensive reporting histories and there will be less publicly-available information concerning such issuers. For these reasons, the Commission solicits comment on whether it would be appropriate to provide for a longer cooling-off period in Exception (xi) in the context of distributions of certain securities, such as securities of an issuer qualified only to use Form S-1, or whether it would be appropriate to consider other criteria in determining the appropriate length of the cooling-off period such as the depth and liquidity of the market for the subject security.

The Commission also is reconsidering whether Exception (xi) should continue to be available solely for over-the-counter transactions. Although such a limitation would be consistent with the original limited purpose of the exception, Rule 415 will permit shelf-registered distributions in both the exchange and over-the-counter markets. As a result, a broker-dealer that has a continuing agreement with an issuer relating to such an offering may be a participant in a distribution, for purposes of Rule 10b-6, for extensive periods of time, irrespective of whether the security in distribution is traded over-the-counter or on an exchange. Because of the quality of available information regarding exchange-traded securities, including last sale information, there appears to be no reason in this context to continue to distinguish participants' purchasing transactions on the basis of whether they are effected in the over-the-counter market market or on an exchange. Moreover, since the only distinction between delayed offerings of securities made pursuant to Rule 415 and other more conventional registered offerings is the fact of shelf-registration and not the distribution mechanisms that will be used. Accordingly, the Commission is proposing to amend Exception (xi) to make it available in all distributions.[35]

2. *Broker-dealers.* If Exception (xi) is amended as proposed, it will permit broker-dealers to bid for or purchase a security in distribution until the later of three business days before the commencement of sales or such other time as they become participants. A broker-dealer that has a continuing

[32] The Commission does not believe that unsolicited purchases by participants as principal prior to the commencement of sales generally present the potential for manipulative abuse to which Rule 10b-6 is addressed.

[33] Pre-effective stabilization has not developed in the past, at least in part, because an underwriting syndicate often was not established ten days before an offering was due to commence. In addition, even if the syndicate were formed at that time stabilizing for ten days would involve placing a significant amount of capital at risk. Moreover, uncertainty may exist ten days before the proposed commencement of an offering as to whether the offering will go forward at all.

[34] *See* note 6, *supra.*

[35] Offerings made pursuant to Rule 415 may be effected through a variety of distribution mechanisms, including fixed priced underwritings, best efforts offerings and, if the issuer qualifies for the use of Form S-3, through brokerage transactions.

agreement with an issuer regarding a shelf distribution would be required to be out of the market three full business days prior to the commencement of any sales of that security in which it participates. Other broker-dealers that participate in sales off the shelf on a more limited basis would be required to be out of the market from the later of three business days before the commencement of sales or the time they agree to participate in sales.[36] The Commission believes that the implementation of this proposed amendment would strike an appropriate balance between the Commission's interest in protecting investors and its interest in permitting issuers to proceed with Rule 415 offerings on a temporary basis.

In order to facilitate the participation of broker-dealers in shelf distributions by issuers, and to reduce the perceived liquidity problems in the over-the-counter market, the staff will not recommend that the Commission take enforcement action under Rule 10b–6 if broker-dealers participating in distributions subject to Rule 10b–6 that are conducted on behalf of issuers or other persons where the issuer is qualified to use new Forms S–2 or S–3 under the Securities Act, conform their trading activity to the proposed amendments from and after the date of this release until the Commission takes final action on these proposals.[37] For the reasons discussed earlier in this release,[38] the staff does not believe that it would be appropriate to extend this interim no-action position in the context of distributions of securities of issuers that are qualified only to use Form S–1.

B. Proposed Exception (xii)

Underlying Rule 10b–6 has been the policy that it is inappropriate for issuers or other persons on whose behalf the distribution is being made ("selling shareholders"), and affiliates of issuers, to purchase the securities of the issuer at times when the securities are the subject of a distribution. These persons may have the incentive to bid up the price of these securities in order to facilitate their sales. Thus, issuers, selling shareholders and their affiliates have been prohibited from bidding for and purchasing such securities from the time they determine to go forward with an offering of their securities which constitutes a distribution until the distribution is completed.

The Commission believes that these prohibitions may be overly restrictive, and is proposing to relax the rule as it applies to issuers and selling shareholders, and to limit coverage of the rule to affiliated purchasers of issuers and selling shareholders, as defined in new paragraph (c)(6) of the rule. An affiliated purchaser would be defined as a person acting in concert with the issuer or other person for the purpose of acquiring the issuer's securities, or an affiliate who, directly or indirectly, controls the issuer's or other person's purchases of such securities, whose purchases are controlled by the issuer or such other person or whose purchases are under common control with those of the issuer or such other person. This definition is a modified form of the term "affiliated purchaser" contained in proposed Rule 13e–2 under the Act.[39] This amendment reflects the view that purchases by affiliates who are acting in concert with the issuer or who control the issuer's purchasing determinations may present more potential for manipulative activity than purchases by other affiliates.

The proposed exception, to be denominated Exception (xii), would permit issuers, selling shareholders or their affiliated purchasers to bid for or purchase the security that is the subject of the distribution and certain related securities [40] until three business days prior to any sales of the securities. Within the three day cooling-off period and thereafter until the completion of the distribution, Rule 10b–6 would prohibit solicited and unsolicited bids for our purchases of the security in distribution and related securities by issuers, selling shareholders and their affiliated purchasers.

Issuers, selling shareholders and their affiliated purchasers may, however, have a special interest in facilitating distributions of their securities. The Commission solicits comment on whether it would be appropriate to distinguish between purchasers and bids made by these persons and those made by broker-dealers and, if so, whether it would be appropriate to impose additional conditions on purchases by these persons, such as imposing a cooling-off period that is longer than three business days.

Because of the special problems that might otherwise arise for issuers engaged in shelf-offerings pursuant to Rule 415, the staff will not recommend that the Commission take enforcement action under Rule 10b–6 if issuers, selling shareholders and their affiliated purchasers rely on proposed Exception (xii) in connection with their purchasing

[36] A determination of the time at which a broker-dealer who is only named in a shelf-registration statement (as opposed to a broker-dealer who has a continuing agreement with the issuer) will be deemed a participant in the issuer's distribution will depend on the facts and circumstances surrounding the broker-dealer's relationship with the issuer and its relationship with other broker-dealers acting on the issuer's behalf. Absent some agreement with the issuer relating to its participation, the Commission does not believe that a broker-dealer should necessarily be deemed to be a participant solely because it is identified in the registration statement as a possible underwriter, particularly if it has not consented to being named. Nevertheless, a broker-dealer that is named as an underwriter in the registration statement would be subject to the three day cooling-off period in connection with any offers and sales in which it acts as underwriter.

One commentator noted that, in the context of at the market offerings contemplated by Rule 415, issuers may decide to sell shares into the exchange markets in normal brokerage transactions effected through its managing underwriter as agent for the issuer. The issuer's managing underwriter may on occasion use a "two-dollar" broker to effect transactions on the exchange. The commentator suggested that the two-dollar broker should not be deemed to be a participant in the distribution by the issuer, as the managing underwriter would be. The Commission believes that a two-dollar broker performing its normal broker functions should not be deemed to be a participant in such distribution absent special arrangements with the issuer or its managing underwriter.

In addition, the Commission reaffirms its position that market professionals who acquire securities directly from the issuer, or from broker-dealers acting for the issuer, for purposes of Rule 10b–6, are not deemed to be involved in a distribution by the issuer if such securities were acquired in the ordinary course of their business and they were not paid any special compensation and had not made any special arrangements with the issuer or its broker. *See* Securities Act Release No. 6334, 46 FR at 42012–3.

[37] This interim no-action position will not, however, be available with respect to the exercise of exchange-traded call options by participants in a distribution of the security underlying such options. As the Commission noted in Securities Exchange Act Release No. 17609 (March 6, 1981), purchases of stock in response to the exercise of exchange-traded options may have significant impact in the market for a security in distribution. Thus, the Commission has taken the position that the exercise of these options is not excepted from Rule 10b–6 under Exception (vii) to the rule and is proposing to codify that position. *See* Section III.D., *infra*. The Commission believes, however, that the prohibitions of Rule 10b–6 should also be amended in this context. Since the market impact occurs after the exercise of the option, it appears that it may be appropriate to subject the exercise of the option to a cooling-off period in excess of three business days. The Commission requests comment on the latest time before commencement of sales in a distribution of the underlying stock that persons subject to Rule 10b–6 should be permitted to exercise exchange-traded call options.

[38] See text and n. 34, *supra*.

[39] *See* Securities Exchange Act Release No. 17222 (October 17, 1980) 45 FR 70890 (1980).

[40] The exception would permit the covered persons to bid for and purchase a security of the same class and series as the security in distribution or any right to purchase such security as provided for in paragraph (a) of Rule 10b–6. In addition, paragraph (b) of Rule 10b–6 provides that when convertibles, warrants or options are the subject of distributions, the securities underlying these securities are also placed in distribution. Proposed Exception (xii) would permit the covered persons to purchase the convertibles, warrants or options and the securities underlying them until three business days before the commencement of sales of these securities.

activity in the context of a distribution involving a shelf-registered offering, from and after the effective date of Rule 415 until the Commission takes final action on these proposals, provided that the issuer is qualified to use Forms S-2 or S-3 under the Securities Act.[41] Since this is a major departure from the present application of Rule 10b-6 in this area, however, the staff will not take this interim no-action position with respect to bids or purchases by these persons during a distribution of securities not effected pursuant to Rule 415.

C. Issuer Repurchases During Distributions Resulting From Mergers

Proposed Exception (xii) is intended to address the issue of repurchases by issuers during distributions, at least in the context of public offerings. Issuer repurchases during distributions pursuant to mergers and other acquisitions, however, may raise different concerns.

The issuance of securities pursuant to a merger in many cases constitutes a distribution for purposes of Rule 10b-6. If the merger does constitute a distribution, it has been deemed to commence at least from the time the issuer reaches an agreement in principle with respect to the merger. Accordingly, subsequent to that time, an issuer may not purchase shares of the security being distributed in connection with the merger (and the other securities covered by Rule 10b-6) unless specifically exempted from or excepted by Rule 10b-6. Under such circumstances, the staff routinely has granted exemptions to permit issuers and their affiliates to purchase shares of the security being distributed in the merger until the earlier of thirty days prior to the shareholder vote on the merger or five business days prior to the mailing of the proxy materials in connection with the merger. In addition, if there are periods during which the market price of the offered security will be a factor in determining the consideration to be paid pursuant to the merger ("valuation period"), the exemption has required the issuer to cease bidding for and purchasing the security five business days prior to and for the duration of any such period.

In light of the new proposed Exception (xii), and the rationale underlying it, the Commission believes that it may be appropriate to reduce the five business day cooling-off period to three business days before the mailing of proxy solicitation materials and prior to valuation periods. The Commission believes that it may be appropriate to codify these positions regarding issuer repurchases during merger distributions if Exception (xii) is adopted in order to eliminate the *ad hoc* exemptive process. During the pendency of these proposals, however, the Commission will continue to grant exemptions on a case-by-case basis to permit purchases during the kinds of distributions discussed above. The Commission solicits comments on the specific proposed changes in the positions concerning issuer repurchases during merger distributions. In addition, the Commission solicits comments on whether an amendment to the rule or an interpretive release discussing the positions outlined above would be more appropriate.

III. Other Amendments to Rule 10b-6

A. Exception (ii)

Exception (ii) to the rule excepts "unsolicited privately negotiated purchases, each involving a substantial amount of such security, effected neither on an exchange nor from or through a broker or dealer." The exception was drafted in response to industry comments made when the rule was under consideration concerning the need to permit the underwriters to purchase, in unsolicited transactions, blocks of securities "overhanging" the market prior to or during a distribution. The provisions of Exception (ii), however, not only permit purchases by underwriters but also allow those purchases to be effected by the issuer, selling shareholders and other participants in a distribution.

Purchases made in reliance on Exception (ii) must not be effected on an exchange. Because exchange last sale tickers afforded publicity to transactions effected on an exchange, it was believed that substantial purchases by persons interested in a distribution could have significant market impact and should not be excepted. Transactions effected in the over-the-counter market or otherwise off an exchange, however, did not raise those concerns since they generally were not publicly disseminated.

In 1972 the Commission adopted Rule 17a-15 [§ 240. 17a-15] under the Act requiring every registered national securities exchange, every national securities association and every broker-dealer not a member of an exchange or association who effected transactions in exchange-traded securities which were not reported by an exchange or association to file with the Commission a plan providing for the collection, processing and dissemination of last sale reports in securities registered or admitted to unlisted trading privileges on an exchange. Rule 17a-15 was subsequently amended and redesignated Rule 11Aa3-1 [§ 240.11Aa3-1]. The joint industry plan filed pursuant to Rule 17a-15 and declared effective by the Commission in May, 1974 requires that all trades in certain exchange-traded securities ("reported securities") wherever effected, be publicly disseminated through the consolidated transaction reporting system ("consolidated system"). Thus, third market trades of reported securities are now included in the consolidated system and are publicized in the same manner as exchange trades. In view of the fact that all transactions in reported securities, whether effected on an exchange or over-the-counter, are now reported in the consolidated system, the staff for some time has interpreted the exception to permit purchases that otherwise qualify under the exception to be effected on an exchange. In its view, the need for the exception has outweighed the potential for manipulative abuse. The Commission is proposing to codify this position. Because of the changes in the reporting system implemented as a result of the implementation of the consolidated system, it is the Commission's belief that the disparate treatment given exchange and over-the-counter transactions that is reflected in Exception (ii) is no longer necessary or justified.

The Commission believes that deleting the requirement that transactions effected in reliance on the exception not be made on an exchange will not increase the opportunity for abuse. Transactions effected in reliance on the exception must be "privately negotiated," and "unsolicited" and not made from or through a broker or dealer.[42] The Commission believes that these requirements are sufficient to preclude the use of Exception (ii) in any systematic scheme to manipulate the price of a security. Accordingly, the Commission proposes to amend Exception (ii) by deleting the requirement that purchases not be effected on an exchange, and by codifying the position that the term "substantial amount," for purposes of the exception, means a block of such security. At such time as final action is taken on these proposals, the Commission intends to codify the staff's position that the term block for purposes

[41] *See* text and n. 34, *supra.*

[42] The staff interprets the phrase "from or through a broker or dealer" to disqualify a broker or a dealer from participating on the "sell" side of a transaction. However, the exception obviously permits a broker-dealer on the "buy" side of the transaction.

of Exception (ii) has the same meaning as the term block in paragraph (a)(16)(B) of proposed Rule 13e-2 under the Act.[43]

B. Exception (iii)

Exception (iii) to the rule provides that purchases by an issuer that are effected more than forty days after the commencement of a distribution for the purpose of satisfying a sinking fund or similar obligation to which the issuer is subject,[44] are not prohibited by the rule. The exception is available only when the issuer effects purchases to satisfy this sinking fund obligation and does not apply to situations in which purchases of the debt security are made for other purposes.[45] Exception (iii) is intended to permit the issuer to fulfill its obligation to satisfy the mandatory sinking fund provisions of the debt instrument. In addition, because the issuer is obligated to purchase pursuant to the sinking fund provisions, it is highly unlikely that those purchases will be effected for the purpose of manipulating the market for the subject security.

Both the purpose of the exception and its formulation imply that Exception (iii) was intended solely to permit satisfaction of sinking fund obligations that are mandatory. Indeed, that has been the staff's interpretation of the exception. Furthermore, although not currently articulated in the rule, the staff's position has been that, in order for an issuer to avail itself of the provisions of Exception (iii) purchases may be made only to satisfy mandatory sinking fund obligations that become due within 12 months of the date of purchase. When the issuer purchases to satisfy sinking fund obligations that become due in the more distant future, the issuer's obligation may no longer outweigh the manipulative potential of such purchases. Thus, the Commission is proposing an amendment to Exception (iii) that will permit an issuer to effect purchases to satisfy sinking fund obligations that are both mandatory and current.

C. Exception (iv)

The Commission is proposing for public comment certain amendments to Exception (iv) to Rule 10b-6. Exception (iv) currently provides that Rule 10b-6 shall not prohibit "odd-lot transactions (and the offsetting round-lot transactions hereinafter referred to) by a person registered as an odd-lot dealer in such security on a national securities exchange who offsets such odd-lot transactions in such security by round-lot transactions as promptly as possible."

Today, there do not remain any registered odd-lot dealers on the national securities exchanges, and the function formerly performed by such dealers is now performed by exchange specialists and other broker-dealers. Accordingly, the Commission proposes to amend Exception (iv) to Rule 10b-6. As amended, Exception (iv) would continue to except from Rule 10b-6 the function formerly performed by registered odd-lot dealers by excepting all "odd-lot transactions and the round-lot transactions associated therewith by a person who acts in a dealer capacity in effecting odd-lot transactions." This exception would recognize that such odd-lot transactions and the accompanying round-lot transactions do not ordinarily raise manipulative concerns that require the absolute bar of Rule 10b-6. The associated round-lot transactions may precede as well as follow the odd-lot transactions that they offset. For the above reasons, the Commission is also proposing corresponding changes in Rules 10b-8(a)(2) and 10a-1(e)(3)-(4).

D. Exception (vii)

Exception (vii) to the rule provides an exception for "the exercise of any right or conversion privilege to acquire any security." This exception is intended to permit transactions involving the exercise or conversion of an issuer's security where the new security is obtained directly from the issuer. Such transactions do not involve any market impact and are thus not subject to the concerns at which Rule 10b-6 is directed.

Recently, the Commission's staff declined to take a "no-action" position to allow the exercise of exchange-traded call options by participants in a distribution of the underlying securities,[46] since such exercises may have a significant market impact on the underlying security.[47]

This position appears consistent with the purpose of Rule 10b-6 and Exception (vii), which were drafted before the advent of exchange-traded options. Accordingly, the Commission, is proposing to amend Exception (vii) by adding the words "directly from the issuer" at the end of the exception.

E. Overallotment Options

In connection with a firm commitment public offering, the underwriters may create a syndicate short position by selling more than the maximum number of securities they have to distribute, *i.e.*, they will oversell the offering.[48] One of the primary purposes for this practice is to anticipate customer cancellations.[49] In order to cover the syndicate short position, the managing underwriters

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[43] Paragraph (a)(16)(B) of proposed Rule 13e-2 would define the term block as a quantity of stock that either

(i) Has a purchase price of $200,000 or more; or

(ii) Is at least 5,000 shares and has a purchase price of at least $50,000; or

(iii) Is at least 20 round lots of the security and totals 150 percent or more of the trading volume for that security or, in the event that trading volume data are unavailable, is at least 20 round lots of the security and totals at least one-tenth of one percent (.001) of the outstanding shares of the security, exclusive of any shares owned by any affiliate.

See Securities Exchange Act Release No. 17222 (October 17, 1980), 45 FR 70890 (1980).

[44] A sinking fund is a reserve of capital that is set aside on an annual basis out of current earnings, for the purpose of providing funds to retire a given bond issue or debt security, in whole or part, prior to its maturity date. The fund is usually controlled by a trustee and may be composed of cash or securities (generally the bonds or other debt security being retired). Payments to the fund are made periodically by the issuer of the subject security and may be in the form of the bonds or debt securities themselves purchased in the open market or called at a price stated in the instrument or cash deposits. The purpose of having a sinking fund is both to protect the debt instrument and to reduce the amount of the issue outstanding and therefore make it easier to repay the balance at maturity. F. Thompson & R. Norguard, *Sinking Funds Their Use and Value* (1967).

[45] *See* no-action letter issued to Glen Alden Corporation, Schenley Industries, Inc. (Feb. 17, 1972).

[46] The amendments to Exception (xi) that the Commission is proposing today would permit the exercise of exchange-traded call options by participants in a distribution of the underlying securities until three business days before the commencement of the distribution. *But see* note 37, *supra*.

[47] *See* Securities Exchange Act Release No. 17609 (March 6, 1981). In that release, the Commission recognized that the degree of market impact depended upon the extent to which those who are assigned exercise notices purchase the underlying stock in the open market, rather than deliver portfolio or borrowed securities.

[48] It is the staff's position that overallotment options are appropriate only in a firm commitment offering in which the underwriter purchases the securities from the issuer or other person on whose behalf the offering is made before it commences sales to the public. The underwriter hence is subject to market risk. In a "best efforts" offering, however, the underwriter has no capital at risk, but acts merely as agent for the seller. Under these circumstances, the underwriter receives compensation from the seller on the basis of the amount of securities actually sold.

[49] Another reason for underwriters to overallot is to create buying power to support the market price so as to facilitate the distribution of securities. As early as 1943, the Director of the Commission's Trading and Exchange Division expressed the view that purchases made to cover overallotments may facilitate the distribution of securities.

* * * A syndicate overallotment is customarily made for the purpose of facilitating the orderly distribution of the offered securities by creating buying power which can be used for the purpose of supporting the market price. Thus, it would appear, in the absence of circumstances indicating the contrary, that purchases made for the purpose of covering the "short position" of the syndicate are effected for the purpose of facilitating the distribution. Securities Exchange Act Release No. 3506 (November 16, 1943).

may negotiate with the issuer to obtain an overallotment option, also known as a Green Shoe option. The option enables the underwriters to require that the issuer sell a specified additional amount of securities which may be used to cover the short position.

Paragraph (c)(3)(B) of Rule 10b–6 specifies the conditions under which an underwriter shall be deemed to have completed its participation in a distribution. The rule provides that an underwriter has completed its participation in distribution when its alloted securities have been distributed and all stabilization arrangements or trading restrictions among underwriters, to which it is a party, have been terminated.[50] It has been the staff's position that, for purposes of the rule, a distribution in connection with a public offering has not been completed until any overallotment option granted in connection with the distribution has been either exercised or cancelled.[51] The rule in its present form does not specifically refer to the effect of an overallotment option on the termination of a distribution of securities. The position is appropriate, however, because securities made available by a seller to an underwriter pursuant to an overallotment option do not constitute a distinct or separate category or class, but are merely additional to the maximum amount of the offered securities and have been sold as such by the underwriter.[52]

Because sales of the securities subject to the overallotment option are made in connection with the distribution of such securities by the underwriter, the underwriter is not deemed to have completed its participation in the distribution until any overallotment option is either exercised or cancelled. The Commission is proposing to codify this requirement in paragraph (c)(3)(B) of the rule.

[50] The purpose of the provision is to permit an underwriter participating in a distribution to determine when it is free from the prohibitions of the rule, allowing it to resume normal operations.

[51] An underwriter with an overallotment option is required to cancel its option prior to purchasing in the open market. If open market purchases are made before the option is exercised, the staff's position is that the option, at that point, has been cancelled. If the underwriter were to exercise the option after making some open market covering purchases (because the market price rises above the option exercise price before the syndicate short position is covered), these market purchases would violate the rule since they had been made before the completion of the distribution (*i.e.*, prior to the cancellation of the option).

[52] Individuals purchasing overalloted securities must receive a prospectus and the shares sold are subject to the underwriting discount.

F. Exception (xiii)

The Commission is proposing for public comment a new exception to Rule 10b–6 that would allow persons subject to the rule to purchase certain investment grade debt securities of an issuer during a distribution of other debt securities of the same class and series of that issuer.

In a no-action letter concerning American Telephone and Telegraph Company ("AT&T") dated February 26, 1975, the staff, with the Commission's concurrence, granted no-action relief to permit the purchase of debt securities of the same class and series as those being distributed if the following conditions were met: (1) the issuer must be subject to the regular reporting requirements of Section 13 or Section 15(d) or the security being purchased must be registered with the Commission pursuant to Section 12(b); (2) the securities being distributed and the securities being purchased must be non-convertible debt securities with fixed interest rates; (3) both the securities being distributed and the securities being purchased must be rated "BBB" or better by Standard and Poor's Corporation and "Baa" or better by Moody's Investor Service, Inc.; and (4) the total outstanding public debt of the issuer must aggregate $100 million or more in face amount.

The Commission is proposing to codify the interpretive position taken in the AT&T letter as new Exception (xiii) to Rule 10b–6, modified to the extent set forth below. This position has been adhered to by the staff since 1975, and is predicated on the belief that it is very difficult, if not impossible, to manipulate the price of investment grade debt. Investment grade debt securities are generally thought to trade in accordance with a concept of relative value, *i.e.*, such securities are to a large degree fungible, so that investors generally evaluate new offerings by looking at comparably rated securities of other issuers. Debt securities that are not of investment grade may pose a greater potential manipulative threat, since those securities tend not to be fungible. Investors are therefore more likely to compare yields of new non-investment grade debt offerings with those of outstanding debt securities of the same issuer.

The Commission is proposing to include as a condition to Exception (xiii) the requirement set forth in the AT&T letter that the issuer be subject to the regular reporting requirements of section 13 or section 15(d) or the security being purchased must be registered with the Commission pursuant to section 12(b). The Commission solicits comment on whether this condition is necessary.

The AT&T letter required that the securities being distributed and the securities being purchased have fixed interest rates. There does not appear to be any basis for excluding from the exception the increasing number of floating rate securities whose interest rates are tied to a benchmark, such as the prime rate or the yield on certain government securities. Accordingly, proposed Exception (xiii) does not contain this condition.

The AT&T letter required that both the securities being distributed and the securities being purchased be rated "BBB" or better by Standard & Poor's Corporation and "Baa" or better by Moody's Investor Service, Inc. In recognition of the fact that other rating organizations have been or may be recognized as "nationally recognized statistical rating organizations" for purposes of Rule 15c3–1(1)(2)(vi)(F) under the Act, relating to the treatment of non-convertible debt securities for net capital purposes, the Commission proposes that this condition be slightly modified to require only that both the debt securities being distributed and those being purchased be rated in one of the four highest rating categories by at least two nationally recognized statistical rating organizations.

The fourth criterion for no-action relief set forth in the AT&T letter—that the outstanding public debt of an issuer must aggregate $100 million or more in face amount—is to some degree inconsistent with the concept that investment grade debt securities trade on the basis of their relative values and financial ratings, but may provide some additional assurance that manipulation of those securities would not be practicable. It appears that the aggregate outstanding public debt requirement does not, however, necessarily achieve the result intended. For example, an issuer may have more than $100 million in outstanding public debt, but less than $1 million outstanding of a particular issue that may be the only one comparable to the security being distributed. Moreover, even a large aggregate amount of outstanding public debt does not ensure the liquidity that makes manipulation difficult, since the debt securities may be held by a very few institutional investors.

Although the Commission is proposing to include the $100 million criterion as a condition to Exception (xiii), comment is solicited on whether this or any other quantity criterion is necessary to achieve the purposes of Rule 10b–6.

Commentators are also invited to suggest an appropriate alternative formulation, perhaps one that combines a lower level of aggregate outstanding public debt with additional criteria responding to the concerns expressed herein.

Since some issuers may desire to use Rule 415 to shelf-register offerings of debt securities immediately after that rule becomes effective, the staff will not recommend that the Commission take enforcement action under Rule 10b-6 if issuers and other participants in a distribution of debt securities make purchases of other classes of debt securities if all of the conditions of proposed Exception (xiii) are met.

In the case of debt securities that do not come within the parameters of proposed Exception (xiii), the staff intends to adhere to the position taken in a no-action letter dated January 11, 1974 concerning Gamble-Skogmo, Inc. In that letter, the staff took the position that outstanding debt securities of an issuer that varied by at least one percent in the coupon interest rate and by at least ten years in the maturity date from those of the debt securities being distributed would not be deemed to be of the "same class and series."

Although the *Gamble-Skogmo* no-action position is not being codified, comments are specifically solicited with regard to whether the staff should modify its position in light of the amendments to Rule 10b-6 being proposed and recent changes in the bond markets, including the dramatic increase in interest rates since 1974[53] and the trend to shorter bond terms.

G. Amendment to Rule 10b-8

When it issues a series of redeemable convertible debentures or redeemable convertible preferred stock (collectively, the "Convertibles"), a company may reserve the right to redeem those securities and generally will commit itself to do so, if at all, at a price that represents a slight premium over the face value of the Convertible.[54] Once an issuer determines to redeem a series of convertible securities and a redemption notice has been issued, holders of the Convertible generally have some period of time ("Redemption Period") during which to make their investment decision. During the Redemption Period, as long as the market price of the underlying security remains substantially above the price at which the Convertible may be converted,[55] holder of Convertibles can be expected to convert them into shares of the underlying security, rather than allow them to be redeemed by the issuer.[56]

Should the market price of the underlying security decline significantly during the Redemption Period, however,[57] holders of Convertibles may find it more profitable to permit the issuer to redeem their securities than to convert them.[58] An issuer, therefore, frequently will enter into an agreement with an underwriter pursuant to which the underwriter will agree to make an offer to purchase Convertibles tendered to it by holders ("Standby Offer"), to convert all such securities into common stock,[59] and thereafter to sell the common stock.[60] The underwriter also will agree to purchase from the issuer, and to resell, the common stock underlying any Convertibles that the issuer actually redeems.

In order to reduce its own exposure to market fluctuations, the underwriter may employ a strategy that is designed to minimize the risk that the underwriter will find itself, at the conclusion of the Redemption Period, holding large amounts of the issuer's common stock. Pursuant to this strategy, the underwriter will sell short shares of the common stock. It may purchase Convertibles, either in the market or pursuant to the Standby Offer and convert them into common stock, as it is obligated to do under the terms of its agreement with the issuer. Finally, the underwriter uses that stock to cover its short position or sells it directly pursuant to a Securities Act registration statement.[61] This strategy is analogous to that employed in connection with "Shields Plan" pro rata rights offerings.[62]

The agreement of the underwriter to participate in the offering of the common stock obtained upon conversion of the Convertibles marks the commencement of its participation in a distribution for purposes of Rule 10b-6. Rule 10b-6 prohibits a participant from bidding for or purchasing the security in distribution, any security that is convertible into or exchangeable for that security or any right to purchase any such security (including the security being redeemed), unless the bid or purchase is excepted by or exempted from the rule.[63]

Rule 10b-6(a)(3)(ix) ("Exception ix") permits participants in a distribution of securities offered through rights issued on a pro rata basis to bid for or purchase those rights in compliance with certain conditions set forth in Rule 10b-8 under the Act.[64] Convertibles, although they generally would be deemed to be "rights to purchase" the underlying common stock in the context of a redemption call by an issuer, are not "rights issued on a pro rata basis," purchases of which are specifically addressed by Rule 10b-8 and Exception (ix). An underwriter therefore must request a written exemption from Rule 10b-6 each time a standby agreement is signed in connection with an issuer's redemption of a series of convertible securities. Because purchases of Convertibles and purchases during rights offerings are both made pursuant to the "Shields Plan" strategy described above, the staff since 1973 has routinely granted these exemption requests, subject to the condition that purchases of Convertibles in the market and all sales of common stock are effected in compliance with Rule 10b-8 as if the

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[53] For example, a 2% difference in coupon rates when prevailing interest rates are 15% may be less significant to an investor comparing two debt securities in making an investment decision than a 1% difference was thought to be when prevailing interest rates were 6%.

[54] The redemption price of a Convertible is specified in the indenture or other similar document under which the Convertible was issued. The redemption price of a convertible debenture is stated as a percentage of the face value of the security, while that of convertible preferred stock generally is stated as a specified dollar amount.

[55] When the market price of the common stock equals or exceeds the conversion price, the Convertible is said to be "in-the-money."

[56] For this reason, redemptions under such circumstances are frequently referred to as "forced conversions" or "forced calls."

[57] The Redemption Period is usuauy approximately 30 days.

[58] The risk that large amount of Convertibles will be redeemed by holders increases as the spread between the market price and the Conversion Price narrows and is especially great during periods when market conditions are volatile.

[59] Although Convertibles are most often convertible into the issuer's common stock, they also may on occasion be exchangeable for shares of preferred stock. *See, e.g., Lehman Brothers Kuhn Loeb, Inc.* (November 25, 1980).

[60] Although the underwriter's transactions would generally be subject to the short swing trading restrictions of Section 16 under the Act, Rule 16b-2(a)(1) excepts transactions by a person who is "engaged in the business of distributing securities and is participating in good faith, in the ordinary course of such business, in the distribution * * *" 17 CFR § 240.16b-2(a)(1).

[61] In addition, the underwriter may engage in stabilizing transactions with respect to the issuer's common stock, which must be conducted in compliance with Rule 10b-7 under the Act.

[62] Shields Plans were developed for use in connection with rights offerings conducted in compliance with Rules 10b-8 under the Act.

[63] Section 240.10b-6(a)(3). Convertibles are deemed by the staff to constitute a "right to purchase" the underlying security for purposes of Rule 10b-6 when it is economically beneficial for the holder of the Convertible to convert it, *i.e.*, when the Convertible would likely be used as a means of obtaining the underlying security. That situation arises whenever the relative prices of the Convertible and the underlying security are such that there is a reasonable expectation that significant amounts of Convertibles will be converted. Such conversions may act to facilitate the distribution of the underlying security.

[64] Section 240.10b-8(d) (A) through (G).

Convertibles were "rights issued on a pro rata basis to security holders."[65]

Because standby redemptions of Convertibles conducted in compliance with the pertinent provisions of Rule 10b–8 appear to present little potential for manipulative abuse, the Commission proposes to amend Rule 10b–8 so that it applies directly to purchases by underwriters of convertible securities in connection with calls for redemptions of such by the issuers thereof. Such purchases then would be specifically excepted from the scope of Rule 10b–6 pursuant to Exception ix.

IV. Regulatory Flexibility Act Considerations

The Regulatory Flexibility Act, which became effective on January 1, 1981, imposes new procedural steps applicable to agency rulemaking which has a "significantly economic impact on a substantial number of small entities."[66] The Chairman of the Commission has certified pursuant to the Regulatory Flexibility Act that the proposed amendments to Rules 10b–6, 10b–8 and 10a–1, if adopted, will not have a significant economic impact on a substantial number of small entities, or any other entities, because the amendments would alleviate the burdens that the Rules presently impose on issuers and certain broker-dealers, and the amendment to Rule 10b–8 would eliminate a layer of regulation imposed in connection with "redemption standby" transactions. Specifically, the amendments to Rule 10b–6 would increase the time period in which broker-dealers can engage in purchasing activity prior to the commencement of a distribution, and would for the first time permit issuers and certain affiliates to bid for or purchase securities that are the subject of a distribution for a certain period prior to the commencement of the offering. The amendment to Rule 10b–8 would have the effect of exempting from regulation under Rule 10b–6 purchases of certain convertible securities made in compliance with Rule 10b–8.

V. Statutory Basis

The proposed amendments to Rule 10b–6 would be adopted under the Act, 15 U.S.C. 78a *et seq.*, and particularly Sections 2, 3, 9(a)(6), 10(a), 10(b), 13(e), 15(c) and 23(a), 15 U.S.C. 78b, 78c, 78i(a)(6), 78j(a), 78j(b), 78m(e), 78o(c) and 78w(a).

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES AND EXCHANGE ACT OF 1934

On the basis of the above discussion and analysis, the Commission is proposing to amend Part 240 of Chapter II of Title 17 of the Code of Federal Regulations as follows:

Note.—The text of the following proposed amendments uses ► arrows to indicate additions and [ ] brackets to indicate deletions:

1. By revising § 240.10a–1(e) (3) and (4) as follows:

§240.10a–1 Short sales

* * * * *

(e) * * *

(3) any sale [by an odd-lot dealer on an exchange with which it is registered for such security, or any over-the-counter sale by a third market maker] ►by a person who acts in a dealer capacity in effecting odd-lot transactions◄ to offset odd-lot orders of customers; (4) any sale [by an odd-lot dealer on an exchange with which it is registered for such security, or any over-the-counter sale by a third market maker] ►by a person who acts in a dealer capacity in effecting odd-lot transactions◄ to liquidate a long position which is less than a round-lot, provided such sale does not change the position of such [odd-lot] dealer [or such market maker] by more than one unit of trading;

* * * * *

2. By amending § 240.10b–6 and by revising (a)(2), (3) (ii), (iii), (iv), (vii), and (xi), and (c)(3)(i), and adding (a)(3) (xii), and (xiii), and (c) (5), and (6) as follows:

§ 240.10b–6 Prohibitions against trading by persons interested in a distribution.

(a) * * *

(2) who is the issuer or other person on whose behalf such a distribution is being made, or ►who is an affiliated purchaser, as that term is defined in paragraph (c)(6) of this Rule, of such issuer or other person, or◄

(3) * * *

(ii) unsolicited privately negotiated purchases, each involving [a substantial amount of such security,] ►at least a block of such security◄ [effected neither on a securities exchange nor] ►that are not effected◄ from or through a broker or dealer; or

(iii) purchases by an issuer effected more than forty days after the commencement of the distribution for the purpose of satisfying a sinking fund or similar obligation to which it is subject ►which becomes due as of a date that does not exceed twelve months from the date of purchase;◄

(iv) odd-lot transactions [() and the [offsetting] round-lot transactions [hereinafter referred to)] ►associated therewith◄ by a person [registered as an odd-lot dealer in such security on a national securities exchange who offsets such odd-lot transactions in such security by round-lot transactions as promptly as possible] ►who acts in a dealer capacity in effecting all-lot transactions;◄

* * * * *

(vii) the exercise of any right or conversion privilege to acquire any security ► directly from the issuer; or◄

* * * * *

(xi) [purchases or bids] ►bids or purchases◄ by an underwriter, prospective underwriter or dealer [otherwise than on a securities exchange, 10 or more business days prior to the proposed commencement of such distribution [or 5 or more business days in the case of unsolicited purchases] ►made prior to the later of (A) 3 business days before the commencement of offers or sales of the securities to be distributed [or the day such offers or sales commence in the case of unsolicited bids or purchases] or (B) such other time as those persons become participants in the distribution,◄ if none of such bids or purchases is for the purpose of creating actual, or apparent, active trading in or raising the price of such security [.] ►;◄ [In the case of securities offered pursuant to an effective registration statement under the Securities Act of 1933 the distribution shall not be deemed to commence for purposes of this clause (a)(3)(xi) of this section prior to the effective date of the registration statement.]

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[65] Market purchases made pursuant to the Standby Offer to holders of Convertibles, other than stabilizing purchases, must be aggregated for the purpose of determining whether paragraphs (d)(A)–(G) of Rule 10b–8 apply to market purchases. Paragraphs (d)(A)–(G) of Rule 10b–8 impose conditions under which bids for or purchases of rights may be made and apply whenever the price of the underlying security is being stabilized or the underwriter has a long position in the underlying security. The restrictions contained in those paragraphs, however, apply only to market purchases of Convertibles.

[66] Although section 601(b) of the Regulatory Flexibility Act defines the term "small entity," the statute permits agencies to formulate their own definitions. The Commission has adopted definitions of the term small entity for purposes of Commission rulemaking in accordance with the Regulatory Flexibility Act. Those definitions, as relevant to this proposed rule-making, are set forth in Rule 0–10, 17 CFR 240.0–19. *See* Securities Exchange Act Release No. 34–18452 (January 28, 1982). An issuer is a "small business" or "small organization" under Rule 0–10 if the issuer, on the last business day of its most recent fiscal year, had total assets of $3,000,000 or less. A broker or dealer generally is a "small business" or "small organization" if it had total capital of less than $500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to § 240.17a–5(d). *See* Rule 0–10(c).

►(xii) bids or purchases by an issuer or other person on whose behalf the distribution is being made, or by any affiliated purchaser [as defined in paragraph (c)(6) of this section] of such issuer or other person if such bids or purchases are made no later than 3 business days before the commencement of any offers or sales of the securities to be distributed, if none of such bids or purchases is for the purpose of creating actual, or apparent, active trading in or raising the price of such security;

(xiii) transactions in debt securities that are not convertible into another security, *provided, however*, that (A) either the issuer of such securities is subject to the regular reporting requirements of Section 13 or section 15(d) of the Act or the securities are registered pursuant to section 12(b) of the Act; (B) both the securities being distributed and the securities to be purchased are rated in one of the four highest rating categories by at least two nationally recognized statistical rating organizations; and (C) all of the outstanding public debt of the issuer amounts in the aggregate to at least $100 million in face amount.◄

* * * * *

(c) * * *

(3) * * *

(i) an underwriter, when he has distributed his participation, including all other securities of the same class acquired in connection with the distribution, and any stabilization arrangements and trading restrictions with respect to such distribution to which he is a party have been terminated; ►*provided, however*, that an underwriter will not be deemed to have completed his participation until any option obtained in connection with that distribution pursuant to which he may purchase from the issuer an additional amount of the securities has been exercised or cancelled◄

* * * * *

►(5) For purposes of this section only, the term "distribution" means an offering of securities, whether or not subject to registration under the Securities Act of 1933, which is distinguished from ordinary trading transactions by the magnitude of the offering or the presence of either special selling efforts and selling methods or the payment of compensation greater than that normally paid in connection with ordinary trading transactions; *provided, however*, that the sale of securities will not constitute a distribution for purposes of this section if the sale has been made in compliance with both the volume limitations and the manner of sale provisions contained in paragraphs (e) and (f) of Rule 144 under the Securities Act of 1933.

(6) The term "affiliated purchaser" means (i) A person acting in concert with the issuer or other person for the purpose of acquiring the issuer's securities, or (ii) An affiliate who, directly or indirectly, controls the issuer's or other person's purchases of such securities, whose purchases are controlled by the issuer or such other person or whose purchases are under common control with those of the issuer or such other person.◄

* * * * *

3. By amending § 240.10b-8 by revising (c)(2) and adding a new sentence at the end of the introductory text of paragraph (d) as follows:

§ 240.10b-8. Distributions through rights.

* * * * *

(c)(2) odd-lot transactions [() and the [off-setting] round-lot transactions [hereinafter referred to)] ►associated therewith◄ by a person [registered as an odd-lot dealer in such security on a national securities exchange who off-sets such odd-lot transactions in such security by round-lot transactions as promptly as possible] ►who acts in a dealer capacity in effecting odd-lot transactions;◄

* * * * *

(d) * * * ►Any conditions imposed upon bids for or purchases of rights in paragraphs (d)(1)—(7) of this section shall also apply to bids for or purchases of convertible securities effected pursuant to a standby underwriting agreement with the issuer in connection with a call for redemption of such securities.◄

* * * * *

VI. Solicitation of Comments

All interested persons are invited to submit written data, views and arguments concerning the foregoing. Persons desiring to make written submissions should submit six copies thereof to George A. Fitzsimmons, Secretary, Securities and Exchange Commission, 500 North Capitol Street, NW., Washington, D.C. 20549, not later than April 30, 1982. Reference should be made to File No. S7-921. All submissions will be made available for public inspection at the Commission's Public Reference Section, Room 6101, 1100 L Street N.W., Washington, D.C.

By the Commission.

Dated: March 3, 1982.

George A. Fitzsimmons,

Secretary.

[FR Doc. 82-6689 Filed 3-12-82; 8:45 am]

BILLING CODE 8010-01-M

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
1735 K STREET NORTHWEST · WASHINGTON, D.C. 20006 · (202) 833-7200

IMPORTANT NOTICE

March 26, 1982

TO: All NASD Members, Trading Departments and Branch Offices

RE: Commencement of Real Time Transaction Reporting in NASDAQ/NMS Securities

Effective April 1, 1982 real time transaction reporting will commence for certain NASDAQ securities that have been designated National Market System (NMS) securities. A list of these securities is attached to this Notice. The Association has received inquiries regarding the ability of a member to include in a single transaction report several transactions in a specific security occurring within a short period of time at the same price (commonly known as "bunching"). In addition, a number of members have sought further explanation as to how to determine the price at which transactions should be reported to the Association. In response to these inquiries, this Notice to Members explains the application of new amendments to the transaction reporting rules which permit bunching under certain circumstances and provides clarification as to the price to be reported.

This notice also announces a change in the hours during which members are required to report transactions in both NASDAQ/NMS and listed securities.

Responsibility to Report Transactions

Attached to this notice is the text of the transaction reporting rules for NASDAQ/NMS securities. These rules have been approved by the Commission and will be effective on April 1, 1982.

It is important to note that these rules apply to every member of the Association irrespective of whether it is a market maker in securities designated as NASDAQ/NMS securities. While market makers in these securities bear principal responsibility for transaction reporting, under certain

circumstances non-market makers will be required to report transactions. As such all members should familiarize themselves with these rules.

Bunching of Transaction Reports

The Board of Governors recognizes that during periods of high trading activity, absent the ability to bunch transactions, members' transation reports may not be reported within ninety seconds of execution. The Board has included provisions in the reporting rules under which a member may bunch transaction reports under certain circumstances. The Board believes these provisions will facilitate timely reporting of transactions and significantly relieve the administrative burdens of reporting transactions on a real time basis. Included in the text of the rules are a number of examples to illustrate bunched transaction reporting. It should be emphasized that these rules provide the only available exceptions to the general rule that each trade should be reported separately. The conditions under which trades may be bunched should be noted carefully to assure reporting consistent with the rules.

Generally, the rules permit bunching in situations involving simultaneous execution of orders, including execution of orders at the market opening; limit orders which are executed when the limit price is reached; and cases where a branch office relays combined customer orders to the firm's trading department for simultaneous execution.

The rules also permit bunching of transactions received by a member which are not simultaneous, but are executed within sixty seconds of the initial execution contained in the bunched report and reported within ninety seconds of the initial execution. In addition, bunching under these circumstances is limited to individual transactions of less than 5,000 shares and transactions not initiated by the member's trading department. Transactions of 5,000 shares or more and those initiated by the trading department are still required to be reported individually. The Commission and the Association will monitor transaction reporting during the Tier 1 phase of NASDAQ/NMS securities to see if revisions to these rules are required.

The bunching provisions do not affect which member is responsible for reporting the transaction. Thus, if a member is not required to report a particular transaction (for example, the "buy" side of a trade between market makers) such trade should not be bunched with transactions required to be reported.

Notwithstanding the bunching provisions, the following trades may not be bunched:

- trades at different prices
- trades which are executed over one minute apart
- non-simultaneous transactions of 5,000 shares or greater
- non-simultaneous transactions solicited by the member's trading department

Price to be Reported

The transaction reporting rules require transactions to be reported at prices which do not include commissions, mark-ups, mark-downs and service charges. The purpose of this method of reporting is to achieve a consistency in transaction reporting and have transaction reports reflect the "wholesale" market for the security. The Association has received several questions from members with regard to the price which is to be reported in certain types of transactions. The Association is issuing this notice to help clarify some of the aspects of trade reporting.

As indicated above, the intention of the reporting requirements is to reflect in the transaction report the "wholesale" market for a particular size transaction. This is accomplished by the requirement that commissions, mark-ups, mark-downs and service charges be excluded from the price reported. Since transactions between members do not involve commissions, mark-ups and mark-downs and are, in fact, wholesale transactions, they are required to be reported at the execution price. In agency transactions, the commission involved in the transaction is required to be disclosed to the customer on the confirmation; therefore, the base price of the transaction disclosed to the customer on the confirmation without the commission should be the price reported.

In principal transactions with customers, the reporting rules require that if a mark-up, mark-down or service charge is charged to the customer, it must be excluded from the reported price. If a member deals with a customer at a wholesale price and does not charge a mark-up or mark-down then the price reported should be the execution price. Transactions executed at a net price which price is at or better than the inside quotation should be reported at the execution price, since for trade reporting purposes there is no mark-up or mark-down. In addition, if a member chooses to disclose its mark-up or service charge on the confirmation to the customer, then the base price disclosed to the customer on the confirmation without the mark-up, mark-down or service charge should be the price reported. In principal transactions with customers where the price disclosed on the confirmation is one price which includes a mark-up, mark-down or service charge, the reporting rules require members to exclude such mark-up, mark-down or service charge in the reported price. The reporting rules require, in such circumstances, that the price reported must be reasonably related to the prevailing market taking into consideration all relevant factors including market conditions, the size of the transaction, the published bids and offers with size at the time of execution and the costs and expenses of execution. <u>It is important to note that sales credits or compensation to salesmen is an internal concern of the member and is not a factor covered in the rule.</u> The amount of sales credit is not a factor since many firms will choose to give a sales credit which is composed of a mark-up plus a portion or all of the wholesale spread.

The objective to be achieved in arriving at a proper price report by excluding the mark-up or mark-down is to determine the wholesale market for the specific transaction (or the execution price for that size transaction in that security if the member sought to execute the transaction in the interdealer market). This determination of course is directly related to the depth and liquidity of the interdealer market in that specific security. For example, if the size of the transaction being executed is equal to or less

than the size being displayed by the market maker quoting the best bid or best offer, then the price to be reported should be at least the best bid or the best offer. In that case, the reported price is clearly the wholesale market for that transaction.

If the size of the transaction is greater than the size of the market maker quoting the best bid or offer, then a judgment has to be made by the member as to the price at which a transaction of that size could have been executed in the interdealer market. This judgment, of course, is directly related to the depth of the market. One indicator of depth would be the number of market makers and the price and size of their quotations. For example, if a member has a transaction of 300 shares and there are ten market makers in the security, three of which are quoting the best bid with a size of 200 shares each, then absent other circumstances the reported price should be at the best bid.

The Association recognizes that the judgment to be made on the price to be reported is much easier in the case of relatively small size transactions than it is in transactions of block size since the depth and liquidity of the market for a relatively small transaction is easier to assess. Disclosure of prices of block transactions, however, is an important aspect of trade reporting and the Association is implementing at the request of the Securities and Exchange Commission a special surveillance program to monitor the prices reported in block transactions. As discussed above, interdealer trades are reported at the execution price and if no mark-up, mark-down or service charge is charged to the customer, the execution price should be reported. In addition, if the mark-up, mark-down or service charge is disclosed on the confirmation, then the base price disclosed to the customer on the confirmation without the mark-up, mark-down or service charge should be the price reported. In determining the price to be reported in block transactions where a mark-up, mark-down or service charge is imposed, but not disclosed on the confirmation, members must make a determination as to the wholesale market for that size transaction in light of the depth and liquidity of the market at the time of execution. For example, in a very high volume, liquid security with a substantial number of market makers, the wholesale price of the block, absent extraordinary circumstances, will most likely be closely related to the inside market for that security. This will most likely occur in the case of the Tier 1 securities where the average monthly volume is at least 600,000 shares per month. However, even in block transactions in Tier 1 securities there may be situations where the proper price to be reported could be away from the quoted market.

For example, a security is quoted in NASDAQ with size displayed as follows:

ABCD	20 1/8	20 1/2	2-2
DLTG	20 1/8	20 1/2	3-3
HIJK	20	20 3/8	
LMNO	20	20 3/8	2-2
PQRS	20	20 1/4	2-2

A member purchases 25,000 shares from an institution at a net confirmation price of 19 1/2 which includes a mark-down. In addition, the daily trading volume for the week preceding the transaction averaged 3,000 shares per day.

quotation halt in the security and executed simultaneously when trading or quotations resume. In no event shall a member delay its opening or resumption of quotations for the purpose of aggregating transactions.

Example: A firm receives, prior to its market opening, several market orders to sell which total 10,000 shares. All such orders are simultaneously executed at the opening at a reported price of 40. REPORT 10,000 shares at 40.

(B) Simultaneous executions by the member of customer transactions at the same price, e.g., a number of limit orders being executed at the same time when a limit price has been reached.

Example: A firm has several customer limit orders to sell which total 10,000 shares at a limit price of 40. That price is reached and all such orders are executed simultaneously. REPORT 10,000 shares at 40.

(C) Orders relayed to the trading department of the reporting member for simultaneous execution at the same price.

Example: A firm purchases a block of 50,000 shares from an institution at a reported price of 40. REPORT 50,000 at 40.
Subsequently, one of the firm's branch offices transmits to the firm's trading department for execution customer buy orders in the security totalling 12,500 shares at a reported price of 40. REPORT 12,500 at 40.
Subsequently, another branch office transmits to the firm's trading department for execution customer buy orders totalling 15,000 shares in the security at a reported price of 40. REPORT 15,000 at 40.

Example: Due to a major change in market conditions, a firm's trading department receives from a branch office for execution customer market orders to sell totalling 10,000 shares. All are executed at a reported price of 40. REPORT 10,000 at 40.

(D) An influx of orders received by the trading department of the reporting member which are impractical to report individually and are executed at the same price within 60 seconds of execution of the initial transaction; provided however, that no individual order of 5,000 shares or more may be aggregated in a transaction report and that the aggregated transaction report shall be made within 90 seconds of the initial execution reported therein. Furthermore, it is not permissible for a member to withhold reporting a trade in

anticipation of aggregating the transaction with other transactions.

Examples: A reporting member receives and executes the following orders at the following times and desires to aggregate reports to the maximum extent permitted under this rule.

First Example

11:01:00 500 shares at 40
11:01:05 500 shares at 40
11:01:10 4,000 shares at 40
11:01:15 500 shares at 40
REPORT: 5,500 shares at 40 within ninety seconds of 11:01.

Second Example

11:01:00 100 shares at 40
11:01:10 6,000 shares at 40
11:01:30 300 shares at 40
REPORT: 400 shares within ninety seconds of 11:01 and 6,000 shares within ninety seconds of 11:01:10 (individual transactions of 5,000 shares or more must be reported separately).

Third Example

11:01:00 100 shares at 40.
11:01:15 500 shares at 40
11:01:30 200 shares at 40
11:02:30 400 shares at 40
REPORT: 800 shares at 40 within ninety seconds of 11:01 and 400 shares at 40 within ninety seconds of 11:02:30 (the last trade is not within sixty seconds of the first and must, therefore, be reported separately).

(2) The reporting member shall identify aggregated transaction reports and order tickets of aggregated trades in a manner directed by the Corporation.

March 26, 1982

TIER 1
NASDAQ/NATIONAL MARKET SYSTEM SECURITIES

1. Apple Computer, Inc.
2. Academy Insurance Group, Inc.
3. American Greetings Corporation
4. American International Group
5. Amarex, Inc.
6. Avantek, Inc.
7. CPT Corporation
8. Color Tile, Inc.
9. Cross and Trecker Corp.
10. Cetus Corporation
11. Economics Laboratory, Inc.
12. El Paso Electric Company
13. Farmers Group, Inc.
14. Flagship Banks, Inc.
15. Graphic Scanning Corporation
16. Hadson Petroleum Corporation
17. Intergraph, Inc.
18. Intel Corporation
19. ISC Systems Corporation
20. Intermedics, Inc.
21. Jerrico, Inc.
22. Life Investors, Inc.
23. MCI Communications Corporation
24. McRae Consolidated Oil & Gas, Inc.
25. Millipore Corporation
26. National Data Corporation
27. Nicklos Oil & Gas Company
28. Network Systems Corporaton
29. Oceaneering International, Inc.
30. Pabst Brewing Company
31. Phoenix Resources Company
32. Seagate Technology
33. Service Merchandise Company, Inc.
34. St. Paul Companies, Inc.
35. Sykes Datatronics, Inc.
36. Tom Brown, Inc.
37. Tandem Computers, Inc.
38. Tampax, Inc
39. Trans-Western Exploration, Inc.
40. United States Surgical Corp.
41. Wetterau, Inc.

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

FORM T

Name of Member ____________________

Address ____________________

Return This Form To:

NASDAQ-New York
Two World Trade Center
New York, New York 10048
Attn: Trade Reports

Trade Date	No. Shares	Security Name	Symbol	Price	Time Executed

Signature of Principal ____________________ Date Prepared ____________________

Instructions

1. Members may report transactions in listed securities or NASDAQ/NMS securities on Form T if: (1) their aggregate daily volume in listed securities or (2) their aggregate daily volume in NASDAQ/NMS securities, does not exceed 1,000 shares or $25,000 on five or more of the previous 10 trading days. If a firm exceeds these amounts or has reason to believe it will exceed them, it must report its trades to the NASD within 90 seconds of execution or designate them as late.

2. This form should also be used to report transactions executed outside normal reporting hours, 10:00 a.m. ET to 4:30 p.m. ET.

3. Members need only report trades for which they have trade reporting responsibility:

   a. In trades between two market makers in the security or two non-market makers, the sell side reports.

   b. In trades between a market maker in the security and a non-market maker, the market maker reports.

   c. In trades between a customer and a member, the member reports.

   d. No trades executed on the floor of an exchange are reported.

4. This form should be returned to:

   NASDAQ - New York
   Two World Trade Center, 98th Floor
   New York, New York 10048
   Attn: Trade Reports

5. Further information on reporting trades in eligible listed securities can be found in Schedule G of the NASD By-Laws. The rules concerning reporting in NASDAQ/NMS securities are contained in Section XIV, Schedule D of the NASD By-Laws. Questions may be directed to NASDAQ - New York at (212) 938-1055.

SCHEDULE D

XIV

Reporting Transactions in NASDAQ National Market System Designated Securities

This Part has been adopted pursuant to Article XVI of the Corporation's By-Laws and applies to the reporting by all members of transactions in NASDAQ/National Market System securities ("designated securities") through the Transaction Reporting System. These securities have been designated pursuant to the "National Market System Securities Designation Plan With Respect to NASDAQ Securities" ("Plan") which has been approved by the Securities and Exchange Commission pursuant to Rule 11Aa2-1.

Section 1 -- Definitions

(a) Terms used in this Part shall have the meaning as defined in the Association's By-Laws and Rules of Fair Practice, Rule 11Aa2-1 and the Plan, unless otherwise defined herein.

(b) "Transaction Reporting System" means the transaction reporting system for the reporting and dissemination of last sale reports in designated securities.

(c) "Registered Reporting Market Maker" means a member of the Association which is registered as a NASDAQ market maker in a particular designated security. A member is a Registered Reporting Market Maker in only those designated securities for which it is registered as a NASDAQ market maker. A member shall cease being a Registered Reporting Market Maker in a designated security when it has withdrawn or voluntarily terminated its quotations in that security or when its quotations have been suspended or terminated by action of the Corporation.

(d) "Non-Registered Reporting Member" means a member of the Association which is not a Registered Reporting Market Maker.

Section 2 -- Transaction Reporting

(a) When and How Transaction Reported

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

(2) Non-Registered Reporting Members shall transmit through the Transaction Reporting System, or if such System is unavailable, via Telex, TWX or telephone to the NASDAQ Department in New York City, within 90 seconds after execution, last sale reports of transactions in designated securities executed during the trading hours of the Transaction Reporting System unless all of the following criteria are met:

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

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

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

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

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

(4) All Members shall report weekly to the NASDAQ Department in New York City, on a form designated by the Board of Governors, last sale reports of transactions in designated securities executed outside the trading hours of the Transaction Reporting System.

(5) All trade tickets for transactions in designated securities shall be time-stamped at the time of execution.

(b) Which Party Reports Transaction

(1) In transactions between two Registered Reporting Market Makers, only the member representing the sell side shall report.

(2) In transactions between a Registered Reporting Market Maker and a Non-Registered Reporting Member, only the Registered Reporting Market Maker shall report.

(3) In transactions between two Non-Registered Reporting Members, only the Member representing the sell side shall report.

(4) In transactions between a member and a customer, the member shall report.

(c) Information To Be Reported

Each last sale report shall contain the following information:

(1) NASDAQ symbol of the designated security;

(2) Number of shares (odd lots shall not be reported);

(3) Price of the transaction as required by paragraph (d) below.

(d) Procedures for Reporting Price and Volume

Members which are required to report pursuant to paragraph (b) above shall transmit last sale reports for all purchases and sales in designated securities in the following manner:

(1) For agency transactions, report the number of shares and the price excluding the commission charged.

Example: SELL as agent 100 shares at 40 plus a commission of $12.50; REPORT 100 shares at 40.

(2) For dual agency transactions, report the number of shares only once, and report the price excluding the commission charged.

Example: SELL as agent 100 shares at 40 plus a commission of $12.50; BUY as agent 100 shares at 40 less a commission of $12.50; REPORT 100 shares at 40.

(3) For principal transactions, except as provided below, report each purchase and sale transaction separately and report the number of shares and the price. For principal transactions which are executed at a price which includes a mark-up, mark-down or service charge, the price reported shall exclude the mark-up, mark-down or service charge. Such reported price shall be reasonably related to the prevailing market, taking into consideration all relevant circumstances including, but not limited to, market conditions with respect to the security, the number of shares involved in the transaction, the published bids and offers with size at the time of the execution (including the reporting firm's own quotation), the cost of execution and the expenses involved in clearing the transaction.

Example: BUY as principal 100 shares from another member at 40 (no mark-down included). REPORT 100 shares at 40.

Example: BUY as principal 100 shares from a customer at 39 7/8, which includes a 1/8 mark-down from prevailing market of 40; REPORT 100 shares at 40.

Example: SELL as principal 100 shares to a customer at 40 1/8, which includes a 1/8 mark-up from the prevailing market of 40; REPORT 100 shares at 40.

Example: BUY as principal 10,000 shares from a customer at 39 3/4, which includes a 1/4 mark-down or service charge from the prevailing market of 40;
REPORT 10,000 shares at 40.

Exception:

A "riskless" principal transaction in which a member that is not a market maker in the security after having received from a customer an order to buy, purchases the security as principal from another member or customer to satisfy the order to buy or, after having received from a customer an order to sell, sells the security as principal to another member or customer to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down.

Example: SELL as principal 100 shares to another member at 40 to fill an existing order;
BUY as principal 100 shares from a customer at 40 minus a mark-down of $12.50;
REPORT 100 shares at 40.

(e) Transactions Not Required To Be Reported

The following types of transactions shall not be reported:

(1) transactions executed through the Computer Assisted Execution System ("CAES");

(2) odd-lot transactions;

(3) transactions which are part of a primary distribution by an issuer or of a registered secondary distribution (other than "shelf distributions") or of an unregistered secondary distribution;

(4) transactions made in reliance on Section 4(2) of the Securities Act of 1933;

(5) transactions where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security, e.g., to enable the seller to make a gift;

(6) purchases or sales of securities effected upon the exercise of an option pursuant to the terms thereof or the exercise of any other right to acquire securities at a pre-established consideration unrelated to the current market.

(f) Aggregation of Transaction Reports

(1) Under the following conditions, individual executions of orders in a security at the same price may be aggregated, for transaction reporting purposes, into a single transaction report.

(A) Orders received prior to the opening of the reporting member's market in the security and simultaneously executed at the opening. Also, orders received during a trading or

In such a situation, absent extraordinary circumstances, a reported price of 20 1/8 for the 25,000 share transaction would probably be viewed as not related to the prevailing market since it is unlikely, taking into consideration only the above factors, that 20 1/8 is the wholesale market for a 25,000 share transaction.

The Board of Governors, during its deliberations prior to the adoption of the trade reporting rule, concluded that a schedule could not be established for the purpose of determining the proper price to be reported in all principal transactions. Consequently, the rule requires that a determination be made by the reporting member in establishing the wholesale market to be reported. Members must be prepared to establish the bases for their determinations of transaction prices reported. If a reported price is questioned, it will be reviewed by a Committee composed of members of the securities industry who will take into consideration the various factors present in the market for the security at the time of execution.

Change in Reporting Hours

The Board of Governors has determined that real time transaction reporting for NASDAQ/NMS securities will be required between the hours of 10:00 a.m. and 4:00 p.m. E.T. This determination was made to coordinate the closing time for last sale trade reports with the 4:00 p.m. closing time of NASDAQ inside quotations which are released to many newspapers.

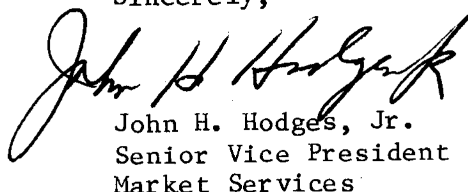
Similarly, in order to maintain consistency and to avoid confusion, the Board determined that third market trade reporting (TMTR) in listed securities will be available during the same hours (10:00 a.m. to 4:00 p.m. E.T.). Prior to this change, the deadline for third market trade reports has been 4:30 p.m. E.T. Commencing on April 1, 1982, all real-time last sale transaction reports for both NASDAQ/NMS securities and over-the-counter transactions in listed securities shall be reported between the hours of 10:00 a.m. to 4:00 p.m. E.T.

Transactions executed outside of these trading hours are to be reported weekly in writing on Form T to the NASDAQ Department in New York City. A copy of Form T is attached to this Notice.

* * *

Questions regarding the trade reporting rules including provisions regarding bunching and prices to be reported should be directed to Don Heizer at (202) 833-7169 or (202) 833-4889.

Sincerely,



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