



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

J. CHARLES PARTEE
MEMBER OF THE BOARD

May 18, 1982

Mr. Gordon S. Macklin
President
National Association of Securities
Dealers, Inc.
1735 K Street, N. W.
Washington, D. C. 20006

Dear Gordon:

I am enclosing, for your convenient reference, a copy of the Board's press release announcing changes to the criteria for inclusion on the List of OTC Margin Stocks. As you may know, the Board considered, in connection with these revisions, the NASD's proposal that the NASD's National List be adopted as the Board's official List of OTC Margin Stocks. We concluded that it would be premature to do so at this time, although such action appears to be a distinct possibility some time in the future. Our principal concerns lie in the areas of adequate dissemination of information concerning the current composition of the list, follow-up surveillance of companies whose securities are included on the National List, commitment of market makers in the NASDAQ system and, as discussed on pages 6 and 7 of the enclosed staff memorandum, possible problems with foreign issues which are traded in NASDAQ but do not file information with the SEC comparable to that required of domestic companies.

There seems to be a serious problem with present newspaper publication of the National List. I understand that many newspapers maintain their own procedures as to which stocks are quoted and that there is no guarantee that the entire list will appear daily in any particular newspaper. This lack of uniformity would present a particular problem for banks and other lenders that would have to determine which stocks are on the List in order to comply with the Board's margin requirements. Since uniform newspaper publication may present an insurmountable problem, perhaps other methods of publication could be explored. For example, you might want to consider publication of a formal list that would be available to the public so that lenders could easily refer to it to determine which NASDAQ securities are marginable. You might also wish to discuss with the SEC the possibility of officially filing the National List with them to give it legal standing as is the case with exchange listings.

I understand that you are in the process of upgrading your NASDAQ listing department, including more intense follow-up procedures to determine a security's compliance with your eligibility standards. Our staff has observed the capabilities of your on-line computer system, NACSIS, and believe that its

Mr. Gordon S. Macklin

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operation, as well as other improvements planned for your listing department will go a long way to ameliorate our concerns that appropriate surveillance and compliance with the newly adopted listing standards is maintained.

Finally, the Board has always been concerned about the depth and breadth of market in connection with credit extensions on over-the-counter securities. A NASDAQ market maker does not have a firm commitment to make a market in a stock comparable to that of a specialist on an exchange and, because of this uncertainty, we have long required that a stock have four market makers throughout the survey period before it is considered for inclusion on the Board's list of OTC Stocks. Only two market makers are required for inclusion on the NASDAQ National List. I note that in your letter dated February 5, 1982, you state that, of the 1,818 securities on the National List, 234 issues had less than four market makers and 71 had less than three. Further study of the market characteristics of these less actively sponsored issues by our respective staffs would seem to me appropriate.

I do appreciate your calling my attention to the problems associated with companies that might voluntarily delist from an exchange but wish to retain margin privileges when they begin to trade in NASDAQ. As you will note, the Board has announced in its Federal Register notice that special consideration for inclusion on the List will be given to companies in such a situation.

The Board will, of course, watch with great interest, the involvement of the National List and its place in the national market system.

Sincerely,

A handwritten signature in black ink, appearing to read "J. Charles Kates". The signature is written in a cursive style with a large, prominent initial "J".

Enclosures