

NASD

National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-80

December 2, 1985

TO: All NASD Members

RE: Final Rules Regarding the Securities and Exchange Commission's Direct Shareholder Communication Program

The Securities and Exchange Commission has adopted the amendments proposed in March to its shareholder communications rules. The amendments, which specify the obligations of brokerage firms and issuers, stipulate:

- That issuers who request a list of nonobjecting security holders from one broker must request it from all brokers with customers who beneficially own the issuer's securities.
- That brokerage firms must provide the beneficial-owner lists to issuers as often as they request the information.
- That issuers may send their annual reports directly to beneficial owners if they notify the broker at the time they submit their search cards.

These amendments were proposed after the SEC postponed the effective date of its direct shareholder communications program from January 1, 1985 to January 1, 1986. The postponement, requested by representatives of the securities industry and issuer community, was intended to give the industry time to determine the reasonable costs of compiling the required information and to implement a system that would provide issuers with the beneficial-owner information in an efficient, timely and effective manner.

To cover the start-up costs of providing issuers with the information, the NASD permitted members to assess a \$.20 per proxy surcharge for the 1985 annual meeting proxy solicitation. If needed, a second surcharge may be permitted for the 1986 proxy season to finance any remaining start-up costs.

When it authorized the deferral, the Commission agreed to clarify the functions of brokerage firms and issuers to ensure the effective implementation of a system of direct communication. In March 1985, the SEC issued a release on its proposals in this area, which the NASD reprinted in Notice to Members 85-30, dated April 22, 1985. The majority of commentators, who represented the legal and

issuer communities and the securities industry, supported the proposals. Accordingly, the Commission adopted the amendments substantially as proposed.

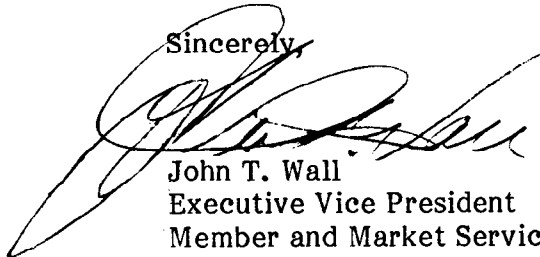
In the release, the SEC recognized the importance of an intermediary to effectively implement its shareholder communications program but did not formally endorse such an intermediary in its rules. Responding to comments on this issue, the Commission has modified the rules to recognize that a brokerage firm may employ an intermediary to act as its designated agent in performing the obligations imposed under the shareholder communications rules.

In addition, the SEC adopted a specified response time in which brokerage firms or their designated intermediary must forward to issuers the list of nonobjecting beneficial owners. The Commission will monitor the program to ensure that it functions properly.

For your convenience, a copy of the SEC's release is enclosed with this notice. The release includes background on the shareholder communications rules and revisions, as well as an overview on implementation.

Any comments or questions regarding this notice should be directed to Thomas P. Mathers of the NASD Communications Group at (202) 728-8267.

Sincerely,

A handwritten signature in black ink, appearing to read "John T. Wall", is written over the word "Sincerely,".

John T. Wall
Executive Vice President
Member and Market Services

Attachment

day time period²⁵ for non-meeting beneficial owner lists. Such an amendment will facilitate communication between registrants and security holders especially involving those corporate actions where time factors are critical.

Proposed Rule 14b-1(c) was structured to provide that a registrant may designate the compilation date for non-meeting lists. Registrant and legal commentators expressed concern, however, that Rule 14b-1(c) was not sufficiently explicit in empowering the registrant, rather than the broker, to designate the compilation date for non-meeting lists. The Commission believes that registrants should be permitted to select the date as of which the non-meeting list is to speak and, accordingly, has clarified that that is the case. Thus, under the rules a registrant may specify the compilation date for a non-meeting list. That date, however, cannot be any earlier than five business days after the broker receives the registrant's request.

In connection with a broker's obligation to provide beneficial owner lists to a registrant, the Commission requested comment on whether a time limit should be specified within which a broker is to provide the registrant with the requested list. An overwhelming majority of the commentators who responded supported imposing a specified turn around response time period. These commentators reasoned that a specific time limit was essential to the operation of the shareholder communication rules and made suggestions for a sufficient time period ranging from five to twenty business days. The Commission agrees that a specified time period is appropriate to ensure that registrants do not receive stale beneficial owner lists that are of little or no value. Accordingly, the Commission has adopted a five business day time period in which brokers are to respond to a registrant's request for non-objecting beneficial owner lists.²⁶ In recognition of the likelihood that a broker may designate an agent to act on its behalf, a note specifying that the time period commences upon receipt by the broker or its designated agent of the registrant's request has been adopted.²⁷

²⁵ Under the shareholder communications rules, business day is defined as it is in Rule 14d-1(b)(6), 17 CFR 240.14d-1(b)(6).

²⁶ In its comment letter, the Ad Hoc Committee, representing members of both the registrant community and securities industry, suggested that a five business day time period was feasible.

²⁷ If a broker designates an agent to act on its behalf, the broker will still be under the obligation to comply with Rule 14b-1(c) and, accordingly, receipt by the intermediary of the registrant's request will be deemed to be receipt by the broker.

Commentators indicated that generally a broker will need three business days to compile and to transmit the beneficial owner information to the intermediary and the intermediary will require two business days to forward the requested beneficial owner information to the registrant.

3. Rule 14b-1(d)

In addition to recognizing that a broker may designate an agent to act on its behalf, Rule 14b-1(d), as adopted makes clear that, without assurance by the registrant, or reimbursement of reasonable expenses, both direct and indirect, incurred in connection with performing its obligations under the rule, a broker need not satisfy its obligations under paragraph (b) and (c) of Rule 14b-1. A broker is obligated, under paragraph (a), however, to supply the information requested by the registrant without regard to reimbursement.

D. Rule 14c-7

The Commission received several comments to its proposed amendments to Rule 14c-7 suggesting that Rule 14c-7, governing the distribution of information statements and annual reports to security holders, be amended to conform with Rule 14a-13. The Commission agrees that such amendments would be useful and, accordingly, has amended Rule 14c-7 to conform, to the extent appropriate, with Rule 14a-13.

V. Statutory Basis and Text of Amendments

These amendments are being adopted pursuant to sections 12, 14, 17 and 23(a) of the Securities Exchange Act of 1934.

List of Subjects in 17 CFR Part 240

Reporting and recordkeeping requirements, Securities.

VI. Text of Amendments

In accordance with the foregoing Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

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

1. The authority citation for Part 240 is amended by adding the following citation (Citations before * * * indicate general rulemaking authority).

Authority: Sec. 23, 48 Stat. 901, as amended; 15 U.S.C. 78w. * * * §§ 240.14a-3, 14a-13, 14b-1 and 14c-7 also issued under sections 12, 14 and 17, 15 U.S.C. 78i, 78n and 78g.

§ 240.14a-3 [Amended]

2. By removing paragraph (d) including Notes 1 and 2 and

redesignating paragraphs (e) and (f) as paragraphs (d) and (e) of § 240.14a-3.

3. By adding § 240.14a-13 to read as follows:

§ 240.14a-13 Obligation of registrants in communicating with beneficial owners.

(a) If the registrant knows that securities of any class entitled to vote at a meeting (or by written consents or authorizations if no meeting is held) with respect to which the registrant intends to solicit proxies, consents or authorizations are held of record by a broker, dealer, bank or voting trustee, or their nominees, the registrant shall:

(1) By first class mail or other equally prompt means: (i) inquire of such record holders: (A) whether other persons are the beneficial owners of such securities and if so, the number of copies of the proxy and other soliciting material necessary to supply such material to beneficial owners; and, in the case of an annual (or special in lieu of the annual) meeting, or written consents in lieu of such meeting, at which directors are to be elected, the number of copies of the annual report to security holders necessary to supply such material to beneficial owners to whom such reports are to be distributed by the broker, dealer, bank, voting trustee or their nominees and not by the registrant; and (B) if the record holder has an obligation under § 240.14b-1(c), whether an agent has been designated to act on its behalf in fulfilling such obligation and, if so, the name and address of such agent; and (ii) indicate to such record holders which are brokers or dealers whether the registrant, pursuant to paragraph (c) of this section, intends to distribute the annual report to security holders to beneficial owners of its securities who have not objected to disclosure of their names, addresses and securities positions.

(2) Make the inquiry at least 20 calendar days prior to the record date of the meeting of security holders, or (i) if such inquiry is impracticable 20 calendar days prior to the record date of a special meeting, as many days before the record date of such meeting as is practicable or (ii) if, consents or authorizations are solicited, and such inquiry is impracticable 20 calendar days before the earliest date on which they may be used to effect corporate action, as many days as is practicable, or (iii) at such later time as the rules of a national securities exchange on which the class of securities in question is listed may permit for good cause shown; and

(3) Shall supply, in a timely manner, the record holders of whom the inquiry is made with additional copies of the

also deliver to brokers for forwarding a sufficient number of copies of the corporate communication in order not to disadvantage those security holders who object to disclosure of their identities to registrants.¹⁹ Further, the Commission believes that even in the case of voluntary communications, the rapid turnover of securities and accompanying non-objecting beneficial owners should be considered in order to avoid the use of outdated non-objecting beneficial owner lists.

Next, consistent with commentators' suggestions, both Rule 14a-13 (b) and (c) were revised to recognize that an intermediary can act as the brokers' agent. Accordingly, when a broker indicates that it has designated an agent, the registrant shall request the beneficial owner list from the agent and reimburse the designated agent for the reasonable expenses²⁰ associated with providing the beneficial owner information. Thus, the Commission anticipates that, if all brokers have designated the intermediary selected by the Ad Hoc Committee, a registrant will need to make only one request for the non-objecting beneficial owner list to that intermediary to satisfy its obligations under Rule 14a-13(b).

4. Rule 14a-13(c)

Proposed Rule 14a-13(c) would have permitted a registrant²¹ to mail the annual reports to security holders directly to those non-objecting beneficial owners that have been identified to them.²² Any registrant choosing to do its own annual report mailing, however, is required, pursuant to paragraph (a), to so inform the broker at the time it made its inquiry for

beneficial owner information under paragraph (a). Commentators overwhelmingly supported the proposal and, accordingly, the Commission adopted this provision substantially as proposed.

The proposing release stated that for reasons of economy, registrants may wish to engage in split mailing, *i.e.*, forwarding the annual report by bulk mail and mailing the proxies and other proxy soliciting material by first class mail. In connection with the use of split mailings, certain registrant commentators addressed the requirement in Rule 14a-3(b) that annual reports must accompany or precede the proxy statement. Commentators requested the Commission to provide specific guidance in this area. Due to the variety of geographic source locations for mailing annual reports and proxy soliciting materials of public reporting companies as well as intended destinations of the materials, however, the Commission is unable to specify exact time periods. Registrants who take steps reasonably calculated to guarantee that the annual reports to security holders accompany or precede the proxy statements will be deemed to have complied with Rule 14a-3(b).²³

The proposing release also solicited comment as to whether Rule 14a-5²⁴ should be amended to provide that when annual reports to security holders are mailed separately from proxy material, all proxy statements should disclose the date the mailing of the annual report to security holders was commenced and should contain instructions on how to obtain a copy of that annual report. The majority of those commentators addressing this issue were registrants who overwhelmingly opposed such an amendment to Rule 14a-5. These commentators based their opposition on the grounds that either no useful purpose would be served or that changes in schedule would prevent accurate disclosure of the date of mailing of the annual report. The Commission agrees and, accordingly, has determined not to amend Rule 14a-5 in this manner.

¹⁹ In *Ash v. GAF Corp.*, 723 F.2d 1090, 1094 (3d Cir. 1983), the Third Circuit held that sending the annual report by third class mail four to five days prior to mailing the proxy statement by first class mail "did not reasonably guarantee that shareholders would receive the annual report at the same time or before the proxy materials. In fact, the procedures made it highly probable that shareholders would receive the annual report after they had received the proxy materials."

²⁴ 17 CFR 240.14a-5.

C. 14b-1 Obligation of Registered Brokers in Connection With the Prompt Forwarding of Certain Communications to Beneficial Owners

1. General

In response to commentators' suggestions, Rule 14b-1 was revised to allow a broker to employ an intermediary to act on its behalf in performing the broker's obligations under the shareholder communications rules. The provision in Rule 14b-1(a) corresponds to that in Rule 14a-13(a)(1) which requires a broker to respond to a registrant's inquiry as to whether the broker has designated an agent to act on its behalf and, if so, to provide the name and address of that designated agent.

2. Rule 14b-1(c)

Under proposed Rule 14b-1(c), a registrant could request the beneficial owner list whenever it wants such a list and the broker, in response to that request, would provide the list. Specifically, the registrant could request the list to be compiled either as of the registrant's record date for its latest annual or special meeting of security holders or, if the request is not made in connection with a meeting, a date no earlier than ten business days after receipt of the registrant's request. Commentators generally supported the proposal to permit registrants to request the lists as often as they wished. One commentator, however, proposed that a maximum number of requests per registrant per year be established. Because these rules are intended to provide for maximum communication between registrants and their beneficial owners, the Commission is of the view that, at this time, registrants should not have limits imposed on the number of requests for beneficial owner lists and, accordingly, has not adopted any such limits.

Proposed Rule 14b-1(c) also provided that non-meeting lists of non-objecting beneficial owners would be compiled as of a date no earlier than ten business days after receipt by the broker of the registrant's request. The proposed ten business day time period was based on the Commission's understanding that broker's back office systems generally do not permit retroactive establishment of beneficial owner lists but, rather, only allow those lists to be established prospectively. Because the securities industry has indicated that this time period should be shortened, the Commission has adopted a five business

¹⁹ Two commentators suggested that the rules require registrants who choose to communicate voluntarily with their non-objecting beneficial owners to deliver sufficient copies of the specific communication to brokers for forwarding to objecting beneficial owners. The Commission does not believe such a change is necessary at this time.

²⁰ Determination of the fee received from the registrant for the non-objecting beneficial owner list will be the subject of proposed SRO rules.

²¹ The shareholder communications rules only apply to those registrants who are subject to the Commission's proxy rules.

²² A few commentators suggested that registrants be permitted to mail proxy cards and proxy soliciting material directly to non-objecting beneficial owners. Consideration of whether to permit registrants to mail proxy soliciting material to non-objecting beneficial owners was not a subject of the Commission's proposal to amend the shareholder communications rules. Further, the Advisory Committee on Shareholder Communications determined not to disrupt the existing system of proxy distribution and voting. See Report on *Improving Communications Between Issuers and Beneficial Owners of Nominee Held Securities* at pp 54-71.

disclosure.⁹ In August 1984, the Commission deferred the original effective date of paragraph (c) from January 1, 1985 to January 1, 1986. The deferral provided additional time to ensure the most effective implementation of the shareholder communications system.¹⁰

Representatives of the securities industry and the registrant community agreed that during this deferral period they would develop and establish both an efficient means of furnishing beneficial owner information to registrants and an appropriate schedule of reimbursement.

In September 1984, the New York Stock Exchange ("the NYSE") appointed the Ad Hoc Committee on Identification of Beneficial Owners. The Ad Hoc Committee, composed of members of both the securities industry and registrant community, was formed to resolve the cost issues and to develop a workable and effective system that would be of maximum use to registrants and not burdensome to brokers. The Ad Hoc Committee now largely has resolved the problems which initially led to the deferral of the effective date of Rule 14b-1(c). The reimbursement of start-up costs issue has been resolved through self-regulatory organization ("SRO") rule changes that permit brokers to assess a \$.20 per proxy surcharge for the 1985 annual meeting proxy solicitation. This surcharge, together with an additional surcharge for the next annual meeting proxy solicitation, will fund the start-up costs associated with furnishing the beneficial owner information to registrants. The second surcharge will fund the balance of the costs not funded by the first \$.20 surcharge and will be the subject of separate SRO rule changes.¹¹ The other cost issue—determination of reasonable costs for maintaining beneficial owner lists—is being addressed by the Ad Hoc Committee and also will be the subject of a separate SRO rule change.

In August 1985, the Ad Hoc Committee drafted a model letter to aid brokers in communicating with their customers in order to ascertain whether or not they object to disclosure of their names, addresses, and securities

positions. The NYSE forwarded that letter to brokers and to the American Stock Exchange and the National Association of Securities Dealers.

To make the system work and to ensure that registrants find the beneficial owner lists useful and meaningful, the Ad Hoc Committee also determined that an intermediary was necessary. By employing an intermediary to compile and to supply beneficial owner lists, registrants will be assured that the lists are compiled in a standardized manner. Moreover, brokers will be assured that the source of the lists will be kept confidential. In addition, economies of scale will be realized by permitting them to delegate this function to an intermediary which will maximize cost savings while minimizing burdens on brokers. The Ad Hoc Committee requested proposals and selected Independent Election Corporation of America ("IECA") to serve as the intermediary between registrants and brokers in supplying lists of beneficial owners. In this function, IECA will be governed by a user board consisting of registrants, brokers, and other industry representatives.

At the time of the deferral of the effective date of Rule 14b-1(c), the Commission agreed to clarify certain aspects of the shareholder communications rules and to take certain additional steps which are the subject of this release.

While the amendments pertain to brokers, the Commission believes that enactment of legislation authorizing the Commission to regulate the proxy processing activities of banks, associations, and other fiduciary entities will realize the full potential of the shareholder communications rules. On July 22, 1985, the House of Representatives passed, by voice vote, legislation entitled the Shareholder Communications Act of 1985 (H.R. 1603). That legislation has been referred to the Securities Subcommittee of the Senate Committee on Banking, Housing, and Urban Affairs. A companion bill (S. 918) was introduced in the Senate on April 16, 1985.

III. Overview of Shareholder Communications Rules

New Rule 14a-13 sets forth two different procedures relating to registrants' obligations in communicating with their beneficial owners, while amended Rule 14b-1 pertains to brokers' obligations in connection with communicating corporate information to beneficial owners. Under the first procedure, registrants are required, pursuant to new Rule 14a-13(a) (formerly Rule 14a-3(d))

to inquire, by means of a search card or otherwise, of their record holders the number of proxies and other proxy soliciting material or annual reports to security holders needed by record holders to forward the material to beneficial owners. The registrant must request this information at least 20 calendar days prior to the record date of the annual meeting and the broker is required, under Rule 14b-1(a), to respond to this request within seven business days of receipt of the request. Upon receipt of the proxy, proxy soliciting material or annual report, the broker is required under Rule 14b-1(b), to forward these materials within five business days of receipt to its customers who are beneficial owners.

Rule 14a-13(b) sets forth the requirements for those registrants who wish to communicate directly with their beneficial owners. If a registrant requests a list of beneficial owners who do not object to disclosure of their names, addresses, and securities positions, it must make that request of all brokers having customers who are beneficial owners of the registrant's securities. Further, a registrant is permitted to request a list of non-objecting beneficial owners more often than once a year and the broker will be required to comply with any such request. These lists would be compiled as of the record date for the registrant's latest annual or special meeting. If no meeting is scheduled and the registrant requests a list of its beneficial owners, that list is to be compiled as of a date to be selected by the registrant that is no less than five business days after the broker receives the request. The broker must forward the beneficial owner information to the registrant no later than five business days after the compilation date of the list, e.g., the record date or other date. For example, if no annual or special meeting is scheduled and the broker receives a registrant's request for the list of beneficial owners on October 15, 1985, the list would be compiled as of a date selected by the registrant that is no earlier than October 22, 1985. The broker, in turn, would be required to forward the beneficial owner list to the registrant by October 29, 1985.

The amendments further provide that, if it chooses, the registrant may mail annual reports directly to non-objecting beneficial owners so long as the registrant notifies the broker when making its initial request for beneficial owner information that the registrant intends to mail the annual report directly to its non-objecting beneficial owners. The registrant would notify the broker of its intention at the time it

⁹ Release No. 34-20021 (July 28, 1983) [48 FR 35082].

¹⁰ Release No. 34-21339 (September 21, 1984) [49 FR 38096].

¹¹ The \$.20 surcharge rule change to the NYSE rules was approved by the Commission on March 28, 1985. Release No. 34-21900 (March 28, 1985) [50 FR 13297]. The Commission approved similar surcharges as part of the rules of the American Stock Exchange and National Association of Securities Dealers. Release No. 34-21915 (April 1, 1985) [50 FR 14069].

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34-22533; IC-14755; File No. S7-13-85]

Facilitating Shareholder Communications

AGENCY: Securities and Exchange Commission.

ACTION: Final rules.

SUMMARY: The Securities and Exchange Commission ("Commission") today announced the adoption of amendments to its shareholder communications rules which govern the process by which registrants communicate with the beneficial owners of securities registered in the name of a broker, dealer or other nominee. The amendments are intended to allow for the most advantageous implementation of the system of direct communication provided under those rules.

EFFECTIVE DATE: New Rule 14a-13 and amended Rules 14b-1 and 14c-7 are effective January 1, 1986.

FOR FURTHER INFORMATION CONTACT: Prior to the effective date, contact Sarah A. Miller, (202) 272-2589, Office of Disclosure Policy, Division of Corporation Finance, Securities and Exchange Commission 450 Fifth Street, NW., Washington, DC 20549. After the effective date, contact Cecilia D. Blye, (202) 272-2573, Office of Chief Counsel, Division of Corporation Finance, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549.

SUPPLEMENTARY INFORMATION: The Commission today announced the adoption of certain rule amendments to Rule 14b-1¹ and 14c-7² and the adoption of Rule 14a-13.³

I. Executive Summary

In March 1985, the Commission proposed certain amendments to refine its shareholder communications rules.⁴

¹ 17 CFR 240.14b-1.

² 17 CFR 240.14c-7.

³ 17 CFR 240.14a-13.

⁴ Release No. 34-21901 (March 28, 1985) [50 FR 13612].

These amendments delineated, in two separate rules, the respective obligations of brokers and registrants. In addition, the proposed amendments provided, among other things, that: (1) If a registrant requests the list of non-objecting security holders, it must request the list from all brokers having customers who are beneficial owners of the registrant's securities; (2) a broker must provide the beneficial owner lists to registrants as often as they request the information, rather than only once a year; and (3) a registrant may mail its annual report to security holders directly to its beneficial owners so long as the registrant notifies the broker at the time it submits a search card or requests beneficial owner information by some other means.⁵ These amendments resulted from the one-year deferral of the effective date (from January 1, 1985 to January 1, 1986) of Rule 14b-1(c) which was agreed to by representatives of the securities industry and registrant community and authorized by the Commission in August 1984.⁶ The deferral was intended to provide more time for the determination of reasonable costs and the implementation of a system to provide registrants with security holder information in an efficient, timely, and effective manner. At the time it authorized the deferral, the Commission agreed to undertake certain steps to clarify the respective functions of brokers and dealers⁷ (hereinafter collectively referred to as "brokers") and registrants to ensure the effective implementation of the system of direct communication.

These proposals generated 41 comment letters.⁸ Commentators,

⁵ In addition to the specific rule amendments, the narrative portion of the proposing release addressed, in connection with the discussion on employment of an intermediary (see discussion *infra* pp. 8, 13, 15), a fourth issue, namely the confidentiality of the source of the beneficial owner lists. See Release No. 34-21901, *supra* note 4, 50 FR at 13613.

⁶ Release No. 34-21339 (September 21, 1984) [49 FR 38006].

⁷ In its proposing release, the Commission clearly intended to require all record holders within its jurisdiction to come within the direct communication system. Accordingly, the term "broker," which as used in the industry usually includes the term "dealer," was used to denote those securities industry personnel who hold securities in nominee name. Because the terms "broker" and "dealer" are separately defined under the Securities Exchange Act, see sections 3(a) (4) and (5) thereof, the Commission believes it is appropriate to revise the rules to clarify that they apply to both brokers and dealers.

⁸ The letters of comment, as well as a copy of the summary of the comment letters prepared by the staff, are available for public inspection and copying at the Commission's Public Reference Room (See File No. S7-13-85).

representing the legal and registrant communities and the securities industry, generally supported the proposals to improve the system of direct communications between registrants and beneficial owners. Accordingly, the Commission is adopting the amendments substantially as proposed.

The proposing release recognized the importance of an intermediary to the effective implementation of the shareholder communications rules. Commentators urged the Commission to recognize explicitly in the rules the role of an intermediary in the shareholder communications system. Also commentators suggested, in response to an inquiry in the proposing release, that the Commission provide for a specified response time in which brokers are to provide registrants with lists of beneficial owners who do not object to disclosure of their names, addresses, and securities positions. In light of these comments, the Commission modified the rules to recognize that a broker may employ an intermediary to act as its designated agent in performing the obligations imposed under the shareholder communications rules and to provide a specified response time in which brokers are to forward to registrants non-objecting beneficial owner lists. Certain other technical clarifying revisions also have been made. The Commission will monitor the workability of its shareholder communications rules to determine whether any further refinements to the rules are necessary and appropriate.

This release discusses the background to the shareholder communications rules and the revisions to those rules. The release also provides an overview regarding implementation of these rules. Persons interested in further information are directed to the text of the amendments and the proposing release.

II. Background

Rule 14b-1 was revised substantially in 1983 pursuant to recommendations of the Advisory Committee on Shareholder Communications, contained in its report, *Improving Communications Between Issuers and Beneficial Owners of Nominee Held Securities*. Paragraph (c) of the rule was adopted to provide a means of direct communication between registrants and their beneficial owners by requiring brokers to provide requesting registrants with the names, addresses, and securities positions of their customers who are beneficial owners of the registrant's securities and who have not objected to such

written consents in lieu of such meeting, at which directors are to be elected, the number of copies of the annual report to security holders, necessary to supply such material to such beneficial owners for whom proxy material has not been and is not to be made available and to whom such reports are to be distributed by the brokers, dealer, bank, voting trustee or their nominees and not by the registrant; and

(2) Indicate to such record holders which are brokers or dealers whether the registrant pursuant to paragraph (c) of this section, intends to distribute the annual report to security holders to beneficial owners of its securities who have not objected to disclosure of their names, addresses and securities positions; and

(3) Supply, in a timely manner, such record holder of whom the inquiry is made with additional copies of the information statement and the annual report to security holders, in such quantities, assembled in such form and at such a place, as the record holder may reasonably request in order to address and send one copy of each to each beneficial owner of securities who is to be furnished with such material by the broker, dealer, bank, voting trustee or their nominees. The number of annual reports supplied shall be sufficient to supply those beneficial owners to whom the report is to be distributed by the broker, dealer, bank, voting trustee or their nominees. The registrant shall, upon the request of such record holder, pay its reasonable expenses for completing the mailing of such material to security holders to whom the material is sent.

Note 1.—If the registrant's list of security holders indicates that some of its securities are registered in the name of a clearing agency registered pursuant to section 17A of the Act (e.g., "Cede & Co.," nominee for the Depository Trust Company), the registrant shall make appropriate inquiry of the clearing agency and thereafter of the participants in such a clearing agency who may hold on behalf of a beneficial owner, and shall comply with the above rule with respect to any such participant.

Note 2.—The requirement for sending an annual report to security holders of record having the same address will be satisfied by sending at least one report to a holder of record at that address provided that those holders of record to whom a report is not sent agree thereto in writing. This procedure is not available to registrants, however, where banks, brokers and dealers and other persons hold securities in nominee accounts or "street names" on behalf of beneficial owners, and such persons are not relieved of any obligation to obtain or send such annual report to the beneficial owners.

Note 3.—The attention of registrants is called to the fact that brokers and dealers have an obligation pursuant to applicable self-regulatory organization requirements to obtain and forward, in a timely manner, (a) information statements to all beneficial owners, and (b) when requested by the registrant annual reports to security holders to beneficial owners for whom such brokers and dealers hold securities.

(b) Any registrant requesting a list of names, addresses and securities positions of beneficial owners of its securities who have not objected to disclosure of such information shall.

(1) Request such list from all brokers and dealers (through their agents) having customers who are beneficial owners of the registrant's securities;

(2) Use the information so furnished exclusively for purposes of corporate communications; and

(3) Upon the request of such brokers and dealers, through their agents, pay the reasonable expenses, both direct and indirect, of providing beneficial owner information.

Note.—A registrant will be deemed to have satisfied its obligations under paragraph (b) of this section by requesting non-objecting beneficial owner lists from a designated agent acting on behalf of the broker or dealer and paying to that designated agent the reasonable expenses of providing the beneficial owner information.

(c) A registrant, at its option, may mail its annual report to security holders to the beneficial owners whose identifying information is provided by brokers and dealers, through their agents, provided that such registrant notifies the brokers and dealers in accordance with paragraph (a) of this section that the registrant will mail the annual report to security holders to the beneficial owners so identified.

By the Commission.

October 15, 1985.

Shirley E. Hollis,

Assistant Secretary.

[FR Doc. 85-25107 Filed 10-21-85; 8:45 am]

proxy, other proxy soliciting material, and/or the annual report to security holders, in such quantities, assembled in such form and at such a place, as the record holder may reasonably request in order to address and send one copy of each to each beneficial owner of securities who is to be furnished with such material by the broker, dealer, bank, voting trustee or their nominees. The number of annual reports supplied shall be sufficient to supply those beneficial owners to whom the report is to be distributed by the broker, dealer, bank, voting trustee or their nominees. The registrant shall upon the request of such record holder, pay its reasonable expenses for completing the mailing of such material to record holders to whom the material is sent.

Note 1.—If the registrant's list of security holders indicates that some of its securities are registered in the name of a clearing agency registered pursuant to section 17A of the Act (e.g., "Cede & Co.," nominee for the Depository Trust Company), the registrant shall make appropriate inquiry of the clearing agency and thereafter of the participants in such clearing agency who may hold on behalf of a beneficial owner, and shall comply with the above paragraph with respect to any such participant.

Note 2.—The attention of registrant is called to the fact that brokers and dealers have an obligation pursuant to § 240.14b-1(b) and applicable self-regulatory organization requirements to obtain and forward, within the time periods prescribed therein, (a) proxy soliciting materials to all beneficial owners, and (b) annual reports to security holders, to all beneficial owners unless the registrant has notified the broker or dealer that it has assumed responsibility to mail such material to non-objecting beneficial owners in which case the broker or dealer shall mail such material to objecting beneficial owners.

(b) Any registrant requesting pursuant to § 240.14b-1(c) a list of names, addresses and securities positions of beneficial owners of its securities who have not objected to disclosure of such information shall:

(1) Request such list from all brokers and dealers (through their agents) having customers who are beneficial owners of the registrant's securities;

(2) Use the information so furnished exclusively for purposes of corporate communications; and

(3) Upon the request of such brokers and dealers, through their agents, pay the reasonable expenses, both direct and indirect, of providing beneficial owner information.

Note.—A registrant will be deemed to have satisfied its obligations under paragraph (b) of this section by requesting non-objecting beneficial owner lists from a designated agent acting on behalf of the broker or dealer and paying to that designated agent the

reasonable expenses of providing the beneficial owner information.

(c) A registrant, at its option, may mail its annual report to security holders to the beneficial owners whose identifying information is provided by brokers and dealers, through their agents, pursuant to § 240.14b-1(c), provided that such registrant notifies the brokers and dealers, at the time a search card requesting the beneficial owner information in accordance with paragraph (a) of this section is sent that the registrant will mail the annual report to security holders to the beneficial owners so identified.

4. By revising § 240.14b-1 to read as follows:

§ 240.14b-1 Obligation of registered brokers and dealers in connection with the prompt forwarding of certain communications to beneficial owners.

A broker or dealer registered under section 15 of the Act shall:

(a) Respond no later than seven business days after receipt of an inquiry made in accordance with § 240.14a-13(a) by or on behalf of a registrant soliciting proxies, consents or authorizations by indicating, by means of a search card or otherwise: (1) The approximate number of its customers who are beneficial owners of the registrant's securities that are held off record by the broker, dealer or its nominees;

(2) The number of its customers who are beneficial owners of the registrant's securities who have objected to disclosure of their names, addresses and securities positions if the registrant has indicated, pursuant to § 240.14a-13(a)(1)(ii), that it will distribute the annual report to security holders to beneficial owners of its securities who have not objected to disclosure of their names, addresses and securities positions; and (3) the identity of its designated agent, if any, acting on behalf of the broker or dealer in fulfilling its obligations under paragraph (c) of this section;

(b) Upon receipt of the proxy, other proxy soliciting material, and/or annual reports to security holders, forward such materials to its customers who are beneficial owners of the registrant's securities no later than five business days after the receipt of the proxy material or annual reports; and

(c) Through its agent or directly, provide the registrant, upon the registrant's request, with the names, addresses and securities positions, compiled as of a date specified in the registrant's request which may be the registrant's record date for its latest annual or special meeting of security

holders, or, if not in connection with a meeting, another date which is no earlier than five business days after receipt of the registrant's request, of its customers who are beneficial owners of the registrant's securities and who have not objected to disclosure of such information. A broker or dealer, through its agent or directly, will be required to transmit the data to the registrant no later than five business days after the record date or other date specified by the registrant.

Note.—Where a broker or dealer employs a designated agent to act on its behalf in performing the obligations imposed on the broker or dealer by paragraph (c) of this section, the five business day time period for forwarding beneficial owner information is calculated from the date the designated agent receives the registrant's request. In complying with the registrant's request for beneficial owner information under paragraph (c) of this section, a broker or dealer need only supply the registrant with the names, addresses and securities positions of non-objecting beneficial owners.

(d) A broker or dealer need not satisfy (1) its obligations under paragraphs (b) and (c) of this section if a registrant does not provide assurance of reimbursement of the broker's or dealer's reasonable expenses, both direct and indirect, incurred in connection with performing the obligations imposed by this section; or (2) its obligation under paragraph (b) of this section to forward annual reports to non-objecting beneficial owners identified by the broker or dealer, through its agent or directly, pursuant to paragraph (c) of this section if the registrant notifies the broker or dealer pursuant to § 240.14a-13(c) that the registrant will mail the annual report to such non-objecting beneficial owners, identified by the broker or dealer and delivered in a list to the registrant pursuant to paragraph (c) of this section.

5. By revising § 240.14c-7 to read as follows:

§ 240.14c-7 Providing copies of material for certain beneficial owners.

(a) If the registrant knows that securities of any class entitled to vote at a meeting, or by written authorizations or consents if no meeting is held, are held of record by a broker, dealer, bank or voting trustee, or their nominees, the registrant shall:

(1) By first class mail or other equally prompt means, (i) inquire of such record holders whether other persons are the beneficial owners of such securities and, if so, the number of copies of the information statement necessary to supply such material to beneficial owners and, in the case of an annual (or special in lieu of the annual) meeting, or

3. Standardized Delivery Format

The proposing release stated that by employing the intermediary to compile and to supply beneficial owner lists, registrants will be assured that the lists are compiled in a standardized manner. Commentators generally endorsed the use of the intermediary to achieve this. Certain commentators, however, suggested that the Commission condition the implementation of the shareholder communications system on specifying a common delivery format. The Commission believes that establishing a mutually acceptable delivery format is best left to the determination of the participants in the shareholder communications system. The Commission would anticipate, however, that any delivery format established would allow registrants flexibility and facilitate corporate communications.

B. 14a-13 Obligations of Registrants in Communicating With Beneficial Owners

1. General.

Proposed Rule 14a-13 consolidated all registrant-related provisions associated with direct shareholder communications, by placing together provisions of Rule 14a-3(d) and the registrant-related provisions of Rule 14b-1(c). As adopted, Rule 14a-13 deals explicitly with solicitations of written consents or authorizations when circumstances warrant separate treatment and to provide that if a special meeting is convened to elect directors in lieu of an annual meeting, an annual report must be furnished to security holders in connection with such meeting. In addition, Rule 14a-13 makes clear that the annual report to security holders is required whether the registrant is soliciting proxies or consents in connection with the annual election of directors and that if it is impracticable for a registrant to make the inquiry for beneficial owner information of the record holder 20 calendar days before the record date of a special meeting then the request must be made as soon as practicable before the record date of such meeting.¹⁶

¹⁶ When the Commission proposed these amendments in Release No. 33-8592 (July 1, 1985) [50 FR 29409], it indicated that these amendments would be adopted at the same time as the shareholder communications proposals were adopted. The comment period for the July proposals closed on September 17, 1985 and, 39 comment letters were received, only one of which addressed these amendments. That comment letter did not oppose the amendments but, rather, suggested clarifications that will be considered as part of the comprehensive review of the proxy rules.

2. Rule 14a-13(a)

Consistent with commentators' suggestions, Rule 14a-13(a)(1) was revised to clarify that the registrant would only need inquire of brokers as to the specific number of copies of the annual report to security holders that ultimately will be distributed by the brokers to beneficial owners pursuant to Rule 14b-1(b). This information would be in addition to the number of copies of the proxy and proxy soliciting material needed to forward to all beneficial owners. To ensure that a registrant knows to whom the request for beneficial owner information is to be made—the broker or its agent—Rule 14a-13(a)(1) was changed to require a registrant to inquire specifically of a broker whether it has designated an agent to act on its behalf and, if so, to ascertain the name and address of that agent. As discussed below, a corresponding change has been made to Rule 14b-1(a). Rule 14a-13(a)(1) also has been changed to clarify that, if it wishes to mail its annual report directly to non-objecting beneficial owners, a registrant has an obligation under Rule 14a-13(c) to notify the broker at the time it makes its inquiry, pursuant to Rule 14a-13(a), that it intends to send copies of its annual report to security holders to non-objecting beneficial owners.

Rule 14a-13(a)(3) has been changed in two respects. First, Rule 14a-13(a)(3) has been revised to clarify that supplying record holders with copies of the proxy, proxy soliciting material, and annual report to security holders and not just the annual report to security holders must be done in a timely manner. Second, commentators expressed concern that Rule 14a-13(a)(3) may be interpreted to require registrants to supply brokers with sufficient copies of the annual report to security holders to mail to all beneficial owners even if the registrant intended to mail the annual reports to security holders directly to its non-objecting beneficial owners. To prevent any such misunderstandings, Rule 14a-13(a)(3) and companion Note 2 have been revised to reflect the possibility that a registrant may mail the annual report to security holders to non-objecting beneficial owners and to require registrants, in those cases, to supply record holders with only the requisite number of copies for distribution by the broker to objecting beneficial owners.

3. Rule 14a-13(b)

As proposed, Rule 14a-13(b) would have required that a registrant request

the list from all brokers having customers who are beneficial owners of the registrant's securities. This requirement was intended to ensure that registrants do not request the security holder lists only from the largest brokers thereby leaving the smaller brokers with no means of recouping expenses associated with maintaining the required information. Commentators generally endorsed the proposal. Of the three commentators who opposed the provision, one commentator suggested that registrants involved in a takeover primarily are interested in holders of large blocks of its securities and should not be required to request non-objecting beneficial owner lists from all brokers.¹⁷ The Commission continues to believe that this provision is necessary for the rule to be fair and effective and has adopted the provision as proposed.

With regard to security holder confidentiality, Rule 14a-13(b)(2) states explicitly that a registrant must use the beneficial owner lists exclusively for purposes of corporate communications. The Commission believes that the inclusion of this provision in the rule adequately addresses concerns regarding security holder confidentiality.

The proposing release also addressed the issue of voluntary communications such as quarterly reports.¹⁸ Due to the importance of this issue the Commission again encourages registrants in connection with their use of beneficial owner lists voluntarily to forward corporate communications to all beneficial owners either directly or through brokers. Accordingly, the Commission believes it is desirable where registrants use the non-objecting beneficial owner lists to mail such communications directly to non-objecting beneficial owners, that they

¹⁷ In tender offers or proxy contests, there is no current requirement under Rules 14a-7, 17 CFR 240.14a-7, and 14d-5, 17 CFR 240.14d-5, for a registrant to turn over a non-objecting beneficial owner list to a requesting security holder. Those rules apply only to lists of record holders and securities position listings of clearing agents. The Commission will consider whether to propose for comment amendments to Rules 14a-7 and 14d-5 which would provide security holders access to lists of non-objecting beneficial owners. Such amendments would provide equal access to these lists and avoid tipping the balance of regulation either in favor of management or in favor of tender offerors or proxy contestants. In the context of tender offers, this change may be consistent with and necessary to effectuate the purposes of the Williams Act. See S. Rep. No. 550, 90th Cong., 1st Sess. 3 (1967), "[t]he bill is designated to require full and fair disclosure for the benefit of investors while at the same time providing the offeror and management equal opportunity to fairly present their case." See also Release No. 33-8022 (February 5, 1979) 44 FR 9956.

¹⁸ Release No. 34-21901 *supra* note 4, at 13614.

submits a search card requesting the beneficial owner information. If so notified by the registrant, a broker would have no obligation in connection with that mailing to forward the annual report to non-objecting beneficial owners but would have, of course, the obligation to forward reports to those beneficial owners who objected to the disclosure of their identities.

The amendments also would provide that, without assurances of reimbursement of reasonable expenses associated with satisfying its obligations with respect to communications with beneficial owners, a broker has no obligation to perform its obligations under Rule 14b-1(b) and (c). The registrant has a corresponding obligation to pay a broker's reasonable expenses associated with providing beneficial owner information.

If a broker has designated an agent or intermediary to act on its behalf in performing its obligations under Rule 14b-1(c), the registrant must make its request for a list of non-objecting beneficial owners to that designated agent. If the broker has designated such an agent, the registrant will learn the agent's identity when it submits, pursuant to Rule 14a-13(a), the search card requesting the number of proxy cards, proxy soliciting material, and annual reports needed by the broker to forward to beneficial owners. The broker, in turn, is required, under Rule 14b-1(a), to identify its agent, if one has been designated. After receiving the registrant's request for beneficial owner information, the agent will notify all brokers of the registrant's request. Brokers will supply the intermediary with the information who then will compile the information in a standardized delivery format and forward it to the registrant. Using the above example, the registrant will make its request to the designated agent for a list of non-objecting beneficial owners. If no annual or special meeting is scheduled and the designated agent receives the registrant's request for the list on October 15, 1985, the list would be compiled as of the date selected by the registrant that is no earlier than October 22, 1985. The designated agent would make the request for a list of non-objecting beneficial owners from all brokers. Brokers, in turn, would forward the requested information to the designated agent who would then compile the list and deliver it to the registrant by October 29, 1985.

IV. Discussion

A. Use of Intermediary

1. Overall Role

Both the Commission and the Ad Hoc Committee believe that an intermediary is necessary to the effective implementation of the shareholder communications system. The intermediary would receive registrants' requests for beneficial owner information and deliver the beneficial owner information supplied by all brokers to the registrants. The proposing release recognized the intermediary's importance in stating that an intermediary will be employed to compile and to supply beneficial owner lists in order to assure standardized delivery format and client confidentiality of brokers.¹² The Commission further noted that economies of scale will be realized by maximizing cost savings while minimizing burdens on brokers by permitting them to delegate this function to an intermediary.¹³

The intermediary would serve as a central processing agent between brokers and registrants in the transmission of lists of non-objecting beneficial owners.¹⁴ In addition, the intermediary would act, on behalf of brokers, in performing all administrative functions required in providing beneficial owner information, including: receiving requests for beneficial owner information from registrants; advising brokers of the record date for a registrant's request; receiving customer lists from brokers; preparing, in a standardized format, lists of non-objecting beneficial owners and billing registrants for fees associated with providing the beneficial owner information.¹⁵

Commentators generally endorsed the use of an intermediary. Several commentators, representing registrants as well as the legal and brokerage communities, suggested, however, that the shareholder communications rules be amended to reflect specifically the intermediary's role in the system of direct communications. Because the Commission believes that the use of an intermediary is necessary for the system to work efficiently, particularly to assure both client confidentiality and

standardized delivery format, the Commission has revised the rules to reflect that (1) brokers may employ an intermediary to act as agent on their behalf in fulfilling the broker's obligations under the shareholder communications rules, and (2) registrants must make their requests to such intermediary. Obviously, registrants will make the request for a non-objecting beneficial owner list to the intermediary only after, the brokers' response to the search card identifying the intermediary is received. Should a broker later designate a new intermediary to act on its behalf, it would be to the benefit of all concerned parties for the broker to notify the registrant of this fact.

While the Commission envisions that brokers generally will choose to employ an agent to assist them in performing their obligations under these rules, and that the agent employed generally will be the intermediary selected by the Ad Hoc Committee, employing an intermediary is not a condition to complying with the shareholder communications rules. Accordingly, the revised rules recognize that a broker may not wish to employ an intermediary to act on its behalf and that, in such cases, the registrant must make the request directly to the broker. The specific amendments reflecting the intermediary's role are discussed below.

2. Client Confidentiality

Of those commentators who addressed the assurance of the client confidentiality function of the intermediary, securities industry commentators endorsed the concept while three registrant and legal commentators opposed it. By employing an intermediary to excise all information identifying specific brokers, brokers will be assured that registrants will obtain only the names, addresses, and securities positions of its beneficial owners. The two registrant commentators who opposed the broker anonymity function of the intermediary maintained that broker confidentiality might limit the usefulness of the beneficial owner information. The Commission believes, however, that disclosure of the broker's identity would not enhance the system of direct communications and, accordingly, has amended Rule 14b-1(c) by adding a note stating, among other things, that a broker or its agent need only supply the registrant with the names, addresses, and securities positions of non-objecting beneficial owners.

¹² Release No. 34-21901 *supra* note 4, at p. 13613.

¹³ *Id.*

¹⁴ It should be noted that a beneficial owner's election to disclose its name, address, and securities position is an election with respect to all registrant's securities in a beneficial owner's account(s) with that broker.

¹⁵ See Ad Hoc Committee letter of June 18, 1985 at pages 3-4 of Exhibit I therein.

NASD

December 2, 1985

TO: All NASD Members and Other Interested Persons

RE: Request for Comments on Proposed Exemption from Free-Riding Interpretation for Conversions of Savings and Loan Associations

LAST DATE FOR COMMENT: JANUARY 2, 1986

The National Association of Securities Dealers, Inc., (NASD) is requesting comments on a proposed amendment that would exempt certain persons purchasing securities in connection with the conversion of a savings and loan association or other organization from mutual to stock ownership from the restrictions of the Interpretation of the Board of Governors, Free-Riding and Withholding (the "Free-Riding Interpretation") under Article III, Section 1 of the NASD Rules of Fair Practice. The proposed amendment, and the history and background leading to its proposal, are discussed in this notice. The text of the amendment is attached.

HISTORY AND BACKGROUND

The Free-Riding Interpretation restricts certain persons from purchasing securities in a public offering if those securities trade at a premium in the immediate aftermarket. The Interpretation prohibits member firms, persons associated with members, immediate family members of such associated persons and other specified persons from purchasing or retaining securities that are part of a "hot" issue. It also requires members to make a bona fide public offering of such securities. To assure compliance with the Interpretation, most firms establish procedures to monitor purchases of new issues. As a practical matter, application of the Interpretation generally restricts the ability of members and their associated persons to purchase new issues.

In recent years, a growing number of savings and loan associations have converted from the mutual form of ownership to stock ownership, issuing securities in the process. Under the rules of the Federal Home Loan Bank Board (FHLBB), federally chartered institutions usually offer their depositors, borrowers and community residents the opportunity to subscribe to their securities prior to any under-

written public offering. In some cases, an association's entire offering will be sold through this subscription process, without participation by a broker-dealer. More commonly, the issuing institution will sell a portion of the offering during the subscription period, with the remaining securities being underwritten and distributed by a broker-dealer. The point at which the broker-dealer becomes involved, and the role performed, varies.

With the proliferation of savings and loan conversions, numerous questions have arisen concerning the ability of persons subject to the Free-Riding Interpretation to purchase securities directly from a savings and loan association during its subscription period. These questions involve several complex issues, especially when a restricted person is entitled under FHLBB rules to purchase securities in the capacity of a depositor or borrower, or when it is unclear whether a broker-dealer will be involved in the offering.

PROPOSED AMENDMENT

In view of these numerous issues, the National Business Conduct Committee (NBCC) of the NASD Board of Governors has reviewed the FHLBB rules, the practices involved in savings and loan conversions and the policy considerations behind the restrictions of the Free-Riding Interpretation. On the basis of this analysis, the NBCC concluded that it is appropriate to exempt certain persons from the Free-Riding Interpretation under specified conditions. In doing so, the NBCC also concluded that it is appropriate to make a distinction between member firms, their associated persons and immediate family members on the one hand and all other restricted persons covered under the Interpretation on the other hand.

Definitions

The proposed amendment would define "conversion offering" as an offering that is part of a plan whereby a savings and loan association or other organization converts from the mutual form to the stock form of ownership. The definition includes offerings by other organizations and would make the language applicable, for example, to conversions by mutual insurance companies.

The amendment would define "eligible purchaser" to mean a person who is eligible to purchase securities directly from the issuer in a savings and loan conversion offering under FHLBB rules and who has a direct relationship with the issuer as a depositor, borrower, officer, director or employee, or serves in a similar capacity.

The terms of savings and loan conversions specify those persons eligible to purchase directly from the issuer in transactions that are not handled by the underwriter. Often, persons eligible to make such purchases can do so prior to the public, underwritten offering. In some cases, the entire offering is distributed to such purchasers. Under FHLBB rules, eligibility to purchase may be extended to residents of the community in which the converting association is located. After careful consideration, the NBCC concluded that it is appropriate to extend the proposed exemption from the Free-Riding Interpretation only to those purchasers who have a direct relationship with the issuer. Thus, depositors, borrowers, officers, directors or employees could claim the exemption (assuming they meet all other criteria), but persons who are eligible under FHLBB rules solely due to their residence could not.

Sales by the Issuer

The proposed amendment provides an exemption from the Free-Riding Interpretation in two different situations:

1. Sales directly by the issuer.
2. Sales by members.

In the first situation, the amendment must address sales by the issuer because the Interpretation otherwise would indirectly prohibit some such sales. When a member or associated person participates in an offering, all transactions that are part of the offering are scrutinized for compliance with the Interpretation. In a typical savings and loan conversion, therefore, sales made directly by the issuer to restricted persons may constitute violations of the Interpretation by NASD members participating in the offering.

The amendment would permit members and associated persons to participate in a conversion offering notwithstanding the fact that the issuer may have sold, or may sell, securities of the offering to persons restricted by the Interpretation. For the exemption to be available, however, any such sales by the issuer must be made only to eligible purchasers as defined. Those purchasers may not be members, their associated persons or immediate family members of associated persons, and the sales must be effected without any direct or indirect participation by a member or associated person. In a savings and loan conversion, therefore, a member could participate in the offering even though the issuer has directly sold shares to restricted persons as long as no sales were made to a member, associated person or immediate family member.

Sales to Members, Associated Persons and Their Immediate Families

The proposed amendment would deal separately with sales to member firms, their associated persons and members of their immediate families and would impose more stringent conditions on the exemption. The NBCC believes there are inherent conflicts of interest between participation in the securities industry and the purchase of "hot" issues, even in the context of the conversion of a savings and loan association. The NBCC concluded that it is necessary to require persons in this category to satisfy additional conditions beyond those previously mentioned for non-securities industry persons.

Subsection (c) would permit members and associated persons to sell securities as part of a conversion offering to members and associated persons and their immediate families if seven conditions are met:

1. Any purchaser must be an eligible purchaser as defined.
2. If a member firm has agreed to serve for compensation as the managing underwriter, appraiser or financial advisor to the issuer in connection with the conversion, neither that member, its associated persons nor their immediate family members can take advantage of the exemption. This restriction becomes applicable when the firm has reached an understanding with the issuer. Persons may claim the exemption prior to the point when such an understanding is reached.

3. Any purchaser claiming the exemption under this category would be required to provide written notice to the issuer of his restricted status under the Free-Riding Interpretation. This condition will enable the issuer and any broker-dealer that may participate in the offering to identify those persons who are subject to the Free-Riding Interpretation to determine whether they have properly satisfied the conditions of this exemption.

4. As a further means of assuring compliance with the conditions of the exemption, associated persons and their immediate family members would be required to provide the person's employer firm with written notice of the subscription.

5. The amount of securities purchased by a person claiming this exemption would be required to be consistent with his or her normal investment history. This limitation is intended to assure that members of the securities industry do not abuse the privilege of purchasing securities in converting institutions to the exclusion of public investors.

6. Securities purchased under this subsection would be restricted from sale, transfer or hypothecation for 90 days following the conclusion of the public offering. This condition is intended to assure that members, their associated persons and immediate families are purchasing the securities for at least a short-term investment and not with the intent of immediately reselling those securities at a premium. The 90-day "lock up" will assure that those persons bear market risk for a reasonable period of time. Such persons thereby would have less incentive to influence prices in the immediate aftermarket to realize profit and would have an incentive to establish a fair public offering price.

7. No member firm, associated person or immediate family member would be permitted to collect solicitation fees from the issuer in connection with purchases made under this subsection. The NBCC concluded that it would be unfair to permit those parties to obtain the potential benefit of an investment under the exemption as well as the payment of a solicitation fee from the issuer.

* * * *

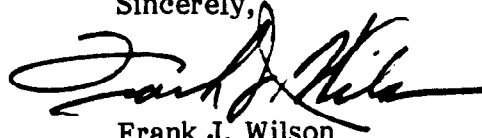
All members and other interested persons are invited to submit comments on the proposed rule. Comments should be received no later than January 2, 1986, and should be directed to:

Mr. James M. Cangiano, Secretary
National Association of Securities Dealers, Inc.
1735 K Street, N.W.
Washington, D.C. 20006

Comments received by the indicated date will be considered by the NBCC and the NASD Board of Governors. Any rule change approved by the Board must be filed with and approved by the Securities and Exchange Commission before becoming effective.

Questions concerning this notice may be directed to Dennis C. Hensley,
Vice President and Deputy General Counsel, at (202) 728-8245.

Sincerely,

A handwritten signature in black ink, appearing to read "Frank J. Wilson", written in a cursive style.

Frank J. Wilson
Executive Vice President
and General Counsel

Attachment

TEXT OF PROPOSED AMENDMENT

Amend the Interpretation of the Board of Governors, Free-Riding and Withholding under Article III, Section 1 of the Rules of Fair Practice by adding at the end thereof the following language:

Conversion Offerings

- (a) Definitions — For purposes of this subsection, the following terms shall have the meanings stated.
- (i) "Conversion offering" shall mean an offering of securities made as part of a plan by which a savings and loan association or other organization converts from the mutual form to the stock form of ownership.
 - (ii) "Eligible purchaser" shall mean a person who is eligible to purchase securities pursuant to the rules of the Federal Home Loan Bank Board or similar agency governing conversion offerings and who has a direct relationship with the issuer as a depositor, borrower, officer, director or employee, or serves in a similar capacity.
- (b) Sales by Issuer — This Interpretation shall not prohibit a member or person associated with a member from participating in a conversion offering notwithstanding the fact that the issuer may have sold or may sell securities of the offering to persons otherwise restricted by this Interpretation, provided that any such sale is made in compliance with all of the following conditions:
- (i) the purchaser is an eligible purchaser;
 - (ii) the purchaser is not a member, a person associated with a member or a member of the immediate family of a person associated with a member; and
 - (iii) the sale is effected without the participation directly or indirectly of a member or person associated with a member.
- (c) Sales to Members, Associated Persons and Immediate Family Members — This Interpretation shall not prohibit a member or person associated with a member from selling securities as a part of a conversion offering to a member, a person associated with a member or a member of the immediate family of a person associated with a member, provided that such sale is made in compliance with all of the following conditions:
- (i) the purchaser shall be an eligible purchaser;
 - (ii) the purchaser shall not be, nor be associated with, nor be a member of the immediate family of a person associated with, a broker-dealer that has agreed to receive compensation for

acting as managing underwriter, appraiser or financial advisor to the issuer in connection with the conversion, or for providing any other service to the issuer;

- (iii) the purchaser shall provide written notice to the issuer, on the subscription form or otherwise, of his or her restricted status under this Interpretation;
- (iv) a person associated with a member shall provide that member with written notice of a purchase by the associated person or a member of his or her immediate family;
- (v) the amount of securities purchased shall be consistent with the purchaser's normal investment history;
- (vi) the securities purchased shall be restricted from sale, transfer or hypothecation for 90 days following the conclusion of the public offering; and
- (vii) neither the purchaser nor the broker-dealer with which he or she or a member of his or her immediate family is associated shall receive any solicitation fees or similar compensation for sales to the broker-dealer, associated person or immediate family member.



National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-82

December 3, 1985

TO: All NASD Members and Municipal Securities Bank Dealers
 ATTN: All Operations Personnel
 RE: Christmas Day - New Year's Day: Trade Date-Settlement Date Schedule

Securities markets and the NASDAQ System will be closed on Wednesday, December 25, 1985, Christmas Day, and Wednesday, January 1, 1986, New Year's Day. "Regular-way" transactions made on the preceding business days will be subject to the settlement date schedule listed below.

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

<u>Trade Date</u>	<u>Settlement Date</u>	<u>Regulation T Date*</u>
December 17	December 24	December 27
18	26	30
19	27	31
20	30	January 2 1986
23	31	3
24	January 2 1986	6
25	MARKETS CLOSED	—
26	3	7
27	6	8
30	7	9
31	8	10
January 1 1986	MARKETS CLOSED	—

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

The foregoing settlement dates should be used by brokers, dealers, and municipal securities dealers for purposes of clearing and settling transactions pursuant to the NASD's Uniform Practice Code and Municipal Securities Rulemaking Board Rule G-12 on Uniform Practice.

Questions regarding the application of these settlement dates to a particular situation may be directed to the Uniform Practice Department of the NASD at (212) 839-6256.

* * * * *

NASD

National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-83

December 10, 1985

TO: All NASD Members and Level 2 and Level 3 Subscribers

RE: NASDAQ National Market System Grows to 2,194 Securities With 16 Voluntary Additions on December 17, 1985

On Tuesday, December 17, 1985, 16 issues are scheduled to join the NASDAQ National Market System, bringing the total number of issues in NASDAQ/NMS to 2,194. These 16 issues, which will begin trading under real-time trade reporting, are entering the NASDAQ/NMS pursuant to the Securities and Exchange Commission's criteria for voluntary designation.

The 16 issues scheduled to join NASDAQ/NMS on Tuesday, December 17, 1985, are:

Symbol*	Company	Location
BNBGV	Bull & Bear Group, Inc. (CI A) WI	New York, NY
COBK	Co-operative Bank of Concord (The)	Concord, MA
ETCIA	Electronic Tele-Communications Inc. (CI A)	Waukesha, WI
HRLN	Harlyn Products, Inc.	Los Angeles, CA
HRES	Horizons Research, Inc.	Cleveland, OH
MAGAF	Magna International, Inc.	Markham, Ontario
MFTN	Metropolitan Federal Savings and Loan Association	Nashville, TN
MBSB	Mt. Baker Bank, A Savings Bank	Bellingham, WA
NATG	National Guardian Corporation (The)	Greenwich, CT

* NASDAQ symbols are proprietary to the National Association of Securities Dealers, Inc.

Symbol*	Company	Location
POSS	Possis Corporation	Minneapolis, MN
PKPS	Poughkeepsie Savings Bank, F.S.B. (The)	Poughkeepsie, NY
QEDXD	Q E D Exploration, Inc.	Denver, CO
SWPA	Southwest National Corporation	Greensburg, PA
STAN	Stanline, Inc.	Norwalk, CA
WFPR	Western Federal Savings Bank	Mayaguez, PR
WBRO	Wood Brothers Homes, Inc.	Denver, CO

The following issues may be included in NASDAQ/NMS prior to the next regularly scheduled phase-in date:

Pending Additions

Symbol*	Company	Location
AMSB	American Savings Bank, F.S.B.	Tacoma, WA
ARKR	Ark Restaurants, Inc.	New York, NY
FUNDA	Colonial Group, Inc. (The) (Cl A)	Boston, MA
DAYS	Days Inns Corporation	Atlanta, GA
FIGIA	Figgie International Holdings, Inc. (Cl A)	Richmond, VA
METS	Met-Coil Systems Corporation	Cedar Rapids, IA
SITVY	Southbrook International Television Company, plc (ADRs)	London, England

NASDAQ/NMS Interim Additions

Symbol*	Company	Date of Entry
ROTC	Rotech Medical Corporation	12/03/85
GWCC	GWC Corporation	12/06/85

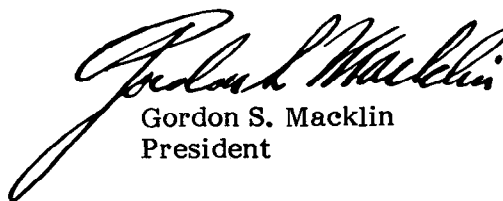
NASDAQ/NMS Deletions

Symbol*	Security	Date
AMRF	Amerford International Corporation	11/27/85
TOPSA	Topsy's International, Inc. (Cl A)	11/27/85
BESIE	Besicorp Group, Inc.	11/29/85
EGLC	Eagle Computer, Inc.	11/29/85
HTIG	Hungry Tiger, Inc.	11/29/85

Symbol*	Security	Date
HACH	Hach Company	12/02/85
NWFN	Northwest Financial Corporation	12/02/85
CSLA	Columbia Savings and Loan Association	12/03/85

Any questions regarding this notice should be directed to Donald Bosc, Assistant Director, NASDAQ Operations, at (202) 728-8043. Questions pertaining to trade reporting rules should be directed to Sharon Bellanger, Market Surveillance, at (202) 728-8206.

Sincerely,



Gordon S. Macklin
President

NASD

notice to members 85-84

December 18, 1985

TO: All NASD Members and Other Interested Persons

RE: New Rule of Fair Practice Relating to Private Securities Transactions

On November 12, 1985, the Securities and Exchange Commission approved a new Article III, Section 40 of the NASD Rules of Fair Practice (SEC Release No. 34-22617). The rule establishes new requirements for the private securities transactions of persons associated with members, and entirely replaces the Private Securities Transactions Interpretation under Article III, Section 27 of the rules. The new rule became effective upon approval by the SEC.

The text of the new rule is attached.

BACKGROUND

The NASD has long been concerned about private securities transactions of persons associated with broker-dealers. These transactions can generally be grouped into two categories:

1. Transactions in which an associated person sells securities to public investors on behalf of another party (e.g., as part of a private offering of limited partnership interests, without the participation of the individual's employer firm); or
2. Transactions in securities owned by an associated person.

The first category of transactions presents serious, regulatory concerns because securities may be sold to public investors without the benefit of supervision or oversight by a member firm and, perhaps, without adequate attention to such regulatory protections as due-diligence investigations and suitability determinations. In some cases, investors may be misled into believing that the associated person's firm has analyzed the security being offered and "stands behind" the product and transaction. The firm, in fact, may be unaware of the associated person's participation in the transaction. Under some circumstances, the firm may be liable for the actions of the associated person even though the firm was not aware of his or her participation in the transaction.

In view of these concerns, the NASD promulgated the Private Securities Transactions Interpretation several years ago. The Interpretation required associated persons to notify their employer firms before participating in private securities transactions. A significant number of associated persons have been disciplined by the NASD for violation of this Interpretation in recent years. The Interpretation enabled firms to exercise better supervision over their associated persons.

At the same time, the Interpretation was a source of substantial confusion, because it addressed only the responsibility of associated persons to notify their member firms of these transactions and did not specifically address the supervisory and oversight responsibilities of the firms. The Board of Governors' Advisory Council and several District Business Conduct Committees requested that the Interpretation be amended to clarify the firms' responsibilities in this area. After careful study, the Board adopted a new rule of fair practice to replace the Interpretation.

The NASD published the proposed rule on private securities transactions for comment in Notice to Members 85-21 (March 29, 1985). In response to the comments received, and following further consideration of the proposed rule by the Board of Governors, the NASD published a slightly revised version for membership vote in Notice to Members 85-54 (August 13, 1985). The new rule was approved by the membership and filed with the SEC, which approved the new rule on November 12, 1985.

Based on an analysis of regulatory problems regarding the handling of private securities transactions, the rule distinguishes between transactions in which the associated person will receive compensation for selling the securities and those for which no compensation will be received. The most serious regulatory concerns relate to situations in which associated persons receive selling compensation and, therefore, have an incentive to execute sales, perhaps without adequate supervision or adequate attention to suitability and due-diligence responsibilities. Some transactions in which associated persons participate without compensation need not be subjected to the same level of scrutiny as other transactions — for example, a salesperson owning stock in a closely held family corporation may wish to transfer that stock to another family member. Whether or not compensation is involved, the new rule specifies the recordkeeping and supervisory responsibilities of member firms.

ANALYSIS OF NEW RULE

Applicability — The new rule, which is attached, applies to any situation in which an associated person of a member proposes to participate in any manner in a private securities transaction.

"Private securities transaction" is defined broadly and generally parallels the concept in the now-deleted Interpretation. Transactions subject to Article III, Section 28 of the NASD Rules of Fair Practice ^{1/} and personal transactions in investment company and variable annuity securities are excluded, as are transactions among immediate family members (as defined in the Interpretation of the Board of

^{1/} Section 28 requires associated persons who handle personal securities transactions through a member other than their employer (the "executing member") to notify the executing member of their employment with another member of the NASD. The executing member is then required to notify the employer member of activity in the associated person's account. See NASD Manual (CCH) ¶2178.

Governors on Free-Riding and Withholding ^{2/}) for which no associated person receives any selling compensation. Because regulatory problems most frequently occur in connection with private placements of new offerings, those transactions are specifically included within the definition of "private securities transaction."

Written Notice — The rule requires associated persons to provide written notice to the employer member before participating in any private securities transaction. The notice must include a detailed description of the proposed transaction and the associated person's proposed role. As the rule treats compensatory and noncompensatory transactions differently, the notice also must state whether the associated person will receive compensation for selling the securities.

Transactions for Compensation — For transactions in which an associated person has or may receive selling compensation, the rule requires that a member firm that receives written notice from an associated person of his or her intent to participate in a private securities transaction must indicate in writing whether the firm approves or disapproves of the associated person's participation in the proposed transaction. If participation is approved, the firm must supervise the associated person's participation to the same extent as if the transaction were executed on behalf of the member firm itself, and record the transaction on the firm's books and records.

If participation is not approved, the associated person is prohibited from participating in the transaction in any manner.

Transactions Not For Compensation — The rule requires that a member receiving notice that an associated person proposes to participate in a transaction, or a series of related transactions, without compensation, provide that associated person with written acknowledgment of the submitted notice.

The rule also gives the employer firm the right to impose conditions on each associated person's participation in noncompensatory transactions. The intention is to give a member firm full discretionary authority to restrict its associated persons' private securities activities, including activities performed on a noncompensatory basis, and to require the associated person to adhere to any condition imposed.

Definition of Selling Compensation — The definition of "selling compensation" plays a key role in the rule. Because the treatment of transactions varies significantly depending upon whether selling compensation is to be received, the definition of "selling compensation" is deliberately broad in its scope.

The definition includes "any compensation paid directly or indirectly from whatever source in connection with or as a result of the purchase or sale of a security." Certain examples are provided, including: commissions; finder's fees; securities; and rights of participation in profits, tax benefits, or dissolution proceeds as a general partner or otherwise. While these examples include some of the most common forms of compensation, the definition is not restricted to these examples. It includes any item of value received or to be received directly or indirectly.

^{2/} NASD Manual (CCH) p. 2045.

It is important to note that the definition of "selling compensation" includes compensation received or to be received by anyone acting as a salesperson or in some other capacity, specifically including the capacity of a general partner. The definition is intended to address a practice in which associated persons function as general partners in the formation of limited partnerships and then sell limited-partnership interests to the public through private securities transactions. Any involvement in a securities transaction by an associated person of an NASD member firm may be subject to the panoply of regulatory requirements applicable to persons associated with a broker-dealer. Participation in transactions as a general partner, therefore, carries with it significant regulatory responsibilities.

* * * *

Questions concerning this notice may be directed to Dennis C. Hensley or Phillip A. Rosen, NASD Office of the General Counsel, at (202) 728-8446.

Sincerely,

A handwritten signature in black ink, appearing to read "Frank J. Wilson", written in a cursive style.

Frank J. Wilson
Executive Vice President
Legal and Compliance

Attachment

NEW RULE OF FAIR PRACTICE*

Section 40: Private Securities Transactions

(a) Applicability — No person associated with a member shall participate in any manner in a private securities transaction except in accordance with the requirements of this section.

(b) Written Notice — Prior to participating in any private securities transaction, an associated person shall provide written notice to the member with which he is associated describing in detail the proposed transaction and the person's proposed role therein and stating whether he has received or may receive selling compensation in connection with the transaction; provided however that, in the case of a series of related transactions in which no selling compensation has been or will be received, an associated person may provide a single written notice.

(c) Transactions for Compensation —

(1) In the case of a transaction in which an associated person has received or may receive selling compensation, a member which has received notice pursuant to Subsection (b) shall advise the associated person in writing stating whether the member:

(A) approves the person's participation in the proposed transaction; or

(B) disapproves the person's participation in the proposed transaction.

(2) If the member approves a person's participation in a transaction pursuant to Subsection (c)(1), the transaction shall be recorded on the books and records of the member and the member shall supervise the person's participation in the transaction as if the transaction were executed on behalf of the member.

(3) If the member disapproves a person's participation pursuant to Subsection (c)(1), the person shall not participate in the transaction in any manner, directly or indirectly.

(d) Transactions Not For Compensation — In the case of a transaction or a series of related transactions in which an associated person has not and will not receive any selling compensation, a member which has received notice pursuant to Subsection (b) shall provide the associated person prompt written acknowledgment of said notice and may, at its discretion, require the person to adhere to specified conditions in connection with his participation in the transaction.

* All language is new. This rule replaces the Private Securities Transactions Interpretation under Article III, Section 27 of the NASD Rules of Fair Practice.

(e) Definitions — For purposes of this section, the following terms shall have the stated meanings:

- (1) "Private securities transaction" shall mean any securities transaction outside the regular course or scope of an associated person's employment with a member, including, though not limited to, new offerings of securities which are not registered with the Commission, provided however that transactions subject to the notification requirements of Article III, Section 28 of the Rules of Fair Practice, transactions among immediate family members (as defined in the Interpretation of the Board of Governors on Free-Riding and Withholding) for which no associated person receives any selling compensation, and personal transactions in investment company and variable annuity securities, shall be excluded.
- (2) "Selling compensation" shall mean any compensation paid directly or indirectly from whatever source in connection with or as a result of the purchase or sale of a security, including, though not limited to, commissions; finder's fees; securities or rights to acquire securities; rights of participation in profits, tax benefits, or dissolution proceeds, as a general partner or otherwise; or expense reimbursements.



National Association of Securities Dealers, Inc.
 1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-85

December 23, 1985

TO: All NASD Members and Municipal Securities Bank Dealers
 ATTN: All Operations Personnel
 RE: Martin Luther King, Jr.'s Day: Trade Date-Settlement Date Schedule

The schedule of trade dates/settlement dates below reflects the observance by the financial community of Martin Luther King, Jr.'s Day, Monday, January 20, 1986. On Monday, January 20, 1986, the NASDAQ System and the exchange markets will be open for trading. However, it will not be a settlement date since many of the nation's banking institutions will be closed.

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

<u>Trade Date</u>		<u>Settlement Date</u>		<u>Regulation T Date*</u>	
January	10	January	17	January	21
	13		21		22
	14		22		23
	15		23		24
	16		24		27
	17		27		28
	20		27		29

It should be noted that January 20, 1986, is considered a business day for receiving customers' payments under Regulation T of the Federal Reserve Board.

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

Securities will not be quoted ex-dividend, and settlements, marks-to-the-market, reclamations, buy-ins and sell-outs, as provided in the Uniform Practice Code, will not be made and/or exercised on January 20.

The foregoing settlement dates should be used by broker-dealers and municipal securities dealers for purposes of clearing and settling transactions pursuant to the Association's Uniform Practice Code and Municipal Securities Rule-making Board Rule G-12 on Uniform Practice.

Questions concerning this notice should be directed to the Uniform Practice Department at (212) 839-6256.

* * * * *



National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-86

December 24, 1985

TO: All NASD Members and Other Interested Persons
RE: Request for Further Comments on a Proposed New Rule Governing the Prompt Payment for Investment Company Shares Sold to Customers by NASD Members

LAST DATE FOR COMMENT: JANUARY 24, 1986

BACKGROUND

In Notice to Members 85-58, dated August 30, 1985, the NASD solicited comments from members and other interested persons on a proposed new rule (new paragraph (m) Article III, Section 26, NASD Rules of Fair Practice) that would govern the prompt payment by NASD members for investment company shares.

The new rule would require NASD members to transmit payments for investment company shares, which such members have sold to customers, to underwriters by the end of the fifth business day after receiving a purchase order from a customer (trade date +5). The rule would also require members who are underwriters to transmit payments for investment company shares, which they have received from customers or other members, to investment company issuers within one business day after receiving such payments (day of receipt +1).

The new rule would replace the NASD Board of Governors interpretation governing the prompt payment by members for shares of investment companies which appears at paragraph 5265 of the NASD Manual.

Forty comment letters were received from members and other interested persons in response to the notice. They contained a variety of comments and suggestions, which were reviewed and discussed by the NASD Investment Companies Committee, a standing committee of the NASD Board of Governors.

The Committee made the following recommendations in response to the major issues raised by commentators. Because one such recommendation involves a major change in the rule as originally proposed, the Committee requested, and the Board of Governors agreed, that the proposed amended rule should be distributed for a further comment period.

Clarification of the term "transmit" in the proposed rule —

The proposed rule will require members to transmit payments by the end of the time periods specified in the rule. Several commentators asked for clarification

of the term "transmit." Would it mean, for example, placing a check in the mail by the end of the last day of the time period specified? It is the intent of the Committee that the term shall mean "payment of funds, by any means, by the end of the specific time periods delineated in the rule."

Adoption of the rule should be delayed until the proposed NSCC centralized and automated system for the clearance and settlement of investment company transactions is operating —

The proposed centralized system being developed by NSCC will provide for automatic settlement in a participant's account with NSCC on trade date +5 business days. Thus, participants processing transactions through NSCC will be in compliance with the provisions of the proposed rule.

The proposed rule, as revised, will primarily affect those members who will not process transactions through the NSCC system since the rule contemplates a somewhat more liberal settlement procedure.

Thus, the Committee believes that there is no reason to delay adoption of the rule.

The rule should require similar prompt payment by investment companies to dealers when investment company shares are liquidated —

Section 22(e) of the Investment Company Act of 1940 governs prompt payment by mutual funds or their agents when shares are liquidated. This section requires a mutual fund to pay liquidation proceeds within seven days after the tender of the security to the fund or its agent.

The Board of Governors prompt payment interpretation has never been applied to the liquidation of fund shares. The Committee believes that delays being experienced in the payment of liquidation proceeds are mainly due to the lack of uniform procedures and the large increase in the number of transactions in recent years. The Committee believes that the introduction of the NSCC automated system will provide the solution to most of the problems that are being experienced in this area of mutual fund activity.

A period of six business days from the order date to the transmittal date is too short —

Many commentators stated that, for members who use the U.S. mail in their investment company activities and who habitually receive checks from customers in payment for their purchases of mutual fund shares, a period of six business days (T +5) from receipt of the order to the transmittal date is too short. They claim that this time period does not take into account the fact that confirmations sometimes are not received by customers until several days after the trade date, customers' checks are often not received promptly and, even if they are, they often take several days to clear.

Imposing a T +5 standard, they claim, would mean that such members, particularly those who are small, would often not have received payment and would not have the necessary capital or the availability of such to enable them to transmit funds by the end of the fifth business day following the trade date.

The result would be that they would either have to make expensive correspondent arrangements, terminate their wire order activities or discontinue mutual fund activities entirely since they would be at a competitive disadvantage with larger well-capitalized members.

The Investment Companies Committee believes the views of these commentators have considerable merit. Hence, it is proposing a major change in the rule that it believes will be responsive to the needs of the members who will not participate in the NSCC system.

The Committee considers that paragraph (1) of the proposed rule should be amended to permit an alternative transmittal date related to the time a member receives payment from a customer.

The Committee recommends that the time a member has to transmit payments be one of the following, whichever is later: (1) the end of the fifth business day after the trade date; or (2) the end of the first business day following receipt of a customer's payment, provided, however, that members will be required to transmit payments by the end of trade date plus seven business days whether or not they have received payment from a customer [Exhibit I, paragraph (m)(1)].

Prompt payment by underwriters to investment companies —

Several members commented that the requirement in paragraph (2) of the proposed rule, which will require members who are underwriters to transmit payments received to issuers by the end of one business day following receipt of such payments, does not provide sufficient time for underwriters engaged in direct retail transactions with customers to ensure that they are in possession of "good funds" because of the time it takes for checks to clear. The Committee believes this should not present a problem to most underwriters and resolved not to amend this section of the proposed rule.

It was also agreed that paragraph (2) of the proposed rule should be amended to reflect the fact that payments are sometimes made by underwriters to the designated agents of issuers and not to the issuing mutual fund [Exhibit I, paragraph (m)(2)].

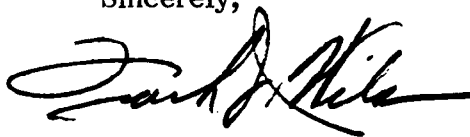
* * * * *

All members and other interested persons are invited to submit written comments on the proposed amended new rule and the proposed rescission of the prompt payment interpretation. Comments must be received no later than January 24, 1986, and should be directed to Mr. James M. Cangiano, Secretary, National Association of Securities Dealers, Inc., 1735 K Street, NW, Washington, D.C. 20006.

Comments received by the indicated date will be considered by the Investment Companies Committee and the NASD Board of Governors. If the proposed rule is approved by the Board, it must then be submitted to the membership for a vote. If approved by the membership, it must be filed with and approved by the Securities and Exchange Commission before becoming effective.

Questions relating to this notice should be directed to A. John Taylor, Vice President, Investment Companies/Variable Contracts, at (202) 728-8328.

Sincerely,



Frank J. Wilson
Executive Vice President
Legal and Compliance

Attachment

**PROPOSED AMENDMENT TO ARTICLE III, SECTION 26
OF THE NASD RULES OF FAIR PRACTICE***

Prompt Payment for Investment Company Shares

- (m) (1) Members shall transmit payments for investment company shares, which such members have sold to customers, to underwriters or their designated agents by ~~[(1)]~~ the end of the fifth business day following receipt of a customer order to purchase such shares [or by (2) the end of one business day following receipt of a customer's payment for such shares, whichever is the later date, provided, however, that members shall transmit payments to underwriters or their designated agents by the end of the seventh business day following receipt of a customer order to purchase such shares whether or not payment has been received from the customer].
- (2) Members who are underwriters shall transmit payments for investment company shares, which such members have received from other members or customers, to investment company issuers [or their designated agents] by the end of the one business day following receipt of such payments.

* New language underlined; additional new language amending original proposed rule bracketed.

NASD

National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-87

December 24, 1985

TO: All NASD Members and Other Interested Persons

RE: Request for Comments on Amendments Concerning Short Sales

LAST DATE FOR COMMENT: JANUARY 30, 1986

The National Association of Securities Dealers, Inc. (NASD), is requesting comment on two proposed amendments to the NASD Rules of Fair Practice. The proposed amendments would require members to (a) mark all customer order tickets "long" or "short" and (b) make an affirmative determination, before accepting a customer's order to sell a security "short," that the security will be either delivered or borrowed prior to settlement date.

The text of the proposed amendments is attached.

Background

At its November 1985 meeting, the Board of Governors discussed the possible need for additional regulation of short selling practices in the over-the-counter market. In the first of a series of actions taken at the November meeting, the Board retained Irving M. Pollack, former SEC commissioner, to conduct a comprehensive study of current short selling practices in the over-the-counter market and to formulate findings and recommendations to serve as the basis for further policy decisions on this issue.

To provide supplemental data for the Pollack study, the Board adopted a new Article III, Section 41 of the NASD Rules of Fair Practice, which will require members to report aggregate "short" positions in NASDAQ securities in all customer and proprietary accounts to the NASD on a monthly basis commencing in early 1986.

The Board also determined to publish for comment amendments to two existing Rules of Fair Practice. The first proposal would amend Article III, Section 21 of the NASD Rules of Fair Practice to require customer order tickets to be marked "long" or "short." Under the proposal, an order may be marked "long" only if

(1) the customer's account is "long" the security; or (2) the member is informed that the customer owns the security and will deliver it within five business days after execution of the order.

The marking of order tickets will assist in the effective surveillance of members' compliance with the second proposal to be published for comment. That proposal is an amendment to the Board of Governors' Interpretation on Prompt Receipt and Delivery of Securities (Interpretation).

The Interpretation currently prohibits members from accepting a customer's sell order, whether "long" or "short," unless (1) the member has possession of the security; (2) the customer's account with the member is "long" the security; (3) the member receives reasonable assurance from the customer that the security will be delivered to it in good deliverable form within five business days after execution of the order; or (4) the security is on deposit in good deliverable form with a member of the NASD, a member of a national securities exchange or any organization subject to state or federal banking regulations, and that instructions have been forwarded to the depository to deliver the securities against payment.

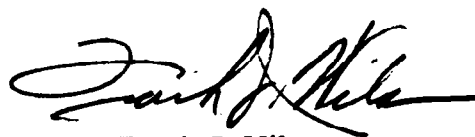
The Board is considering amending the Interpretation to distinguish between "long" and "short" customer sell orders and to adopt different requirements for members accepting "short" customer sell orders. Under the proposed amendment, a member would be prohibited from accepting a "short" sale order from a customer unless the member makes an affirmative determination that it will receive delivery of the security from the customer or that it can borrow the security on behalf of the customer for delivery by settlement date.

All members and other interested persons are invited to submit comments on the proposed rule. Comments should be received no later than January 30, 1986, and should be directed to:

Mr. James M. Cangiano, Secretary
National Association of Securities Dealers, Inc.
1735 K Street, N.W.
Washington, D.C. 20006

Questions concerning this notice may be directed to Mary S. Head, Office of General Counsel, at (202) 728-8284.

Sincerely,

A handwritten signature in black ink, appearing to read "Frank J. Wilson", written in a cursive style.

Frank J. Wilson
Executive Vice President
and General Counsel

Attachment

**1. PROPOSED AMENDMENT TO ARTICLE III, SECTION 21
OF THE RULES OF FAIR PRACTICE**

Add a new subsection (b) and renumber existing subsections:

Information on orders

- (b) A person associated with each member shall indicate on the memorandum for each customer order for the sale of any security whether the order is "long" or "short." An order shall be marked "long" only if (1) the customer's account is "long" the security involved or (2) the member is informed that the customer owns the security and will deliver it within five (5) business days after execution of the order.

**2. AMENDMENT TO THE BOARD OF GOVERNORS' INTERPRETATION
ON PROMPT RECEIPT AND DELIVERY OF SECURITIES**

(New language is underscored; language to be deleted is bracketed.)

It shall be deemed a violation of Article III, Section 1 of the Rules of Fair Practice of the Association for a member to violate the provisions of the following interpretation thereof:

- (a) Purchases: No member may accept a customer's purchase order for any security unless it has first ascertained that the customer placing the order or its agent agrees to receive securities against payment in an amount equal to any execution, even though such an execution may represent the purchase of only a part of a larger order.

(b) Sales:

(1) Long Sales

No member or persons associated with a member shall accept [execute] a long sale [sell] order for any customer in any security unless:

- (a) The member has possession of the security;
- (b) The customer is long in his account with the member;
- (c) Reasonable assurance is received by the member, or person associated with a member, from the customer that the security will be delivered to it in good deliverable form within five (5) business days of the execution of the order; or
- (d) The security is on deposit in good deliverable form with a member of the Association, a member of a national securities exchange, a broker/dealer registered with the

Securities and Exchange Commission, or any organization subject to state or federal banking regulations and that instructions have been forwarded to that depository to deliver the securities against payment.

(2) "Short" Sales

No member or person associated with a member shall accept a "short" sale order for any customer in any security unless the member makes an affirmative determination that it will receive delivery of the security from the customer or that it can borrow the security on behalf of the customer for delivery by settlement date.



National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-88

December 31, 1985

TO: All NASD Members and Level 2 and Level 3 Subscribers

RE: NASDAQ National Market System Grows to 2,214 Securities With 29 Voluntary Additions on January 7, 1986

On Tuesday, January 7, 1986, 29 issues are scheduled to join the NASDAQ National Market System, bringing the total number of issues in NASDAQ/NMS to 2,214. These 29 issues, which will begin trading under real-time trade reporting, are entering the NASDAQ/NMS pursuant to the Securities and Exchange Commission's criteria for voluntary designation.

The 29 issues scheduled to join NASDAQ/NMS on Tuesday, January 7, 1986, are:

Symbol*	Company Name	Location
BNHB	BNH Bancshares, Inc.	New Haven, CT
BISC	Barrister Information Systems Corporation	Buffalo, NY
BSTL	Birmingham Steel Corporation	Birmingham, AL
BRAN	Brand Insulations, Inc.	Park Ridge, IL
CPFD	Capital Federal Savings & Loan Association	Sacramento, CA
CWLD	Child World, Inc.	Avon, MA
CEXX	Circle Express, Inc.	Indianapolis, IN
CNVLZ	City Investing Company Liquidating Trust	New York, NY
CFUR	Cochrane Furniture Company, Inc.	Lincolnton, NC

* NASDAQ symbols are proprietary to the National Association of Securities Dealers, Inc.

Symbol*	Company	Location
CFFS	Columbia First Federal Savings & Loan Association	Washington, D.C.
CNCO	Conseco, Inc.	Carmel, IN
DEST	DEST Corporation	Milpitas, CA
DEFI	Defiance Precision Products, Inc.	Defiance, OH
EBMI	E & B Marine, Inc.	Edison, NJ
EAVN	Eaton Vance Corporation	Boston, MA
GNTX	Gentex Corporation	Zeeland, MI
GWSH	George Washington Corporation	Jacksonville, FL
HACH	Hach Company	Loveland, CO
MRCY	Mercury General Corporation	Los Angeles, CA
NYMG	New York Marine and General Insurance Company	New York, NY
PECN	Publishers Equipment Corporation	Carrollton, TX
RWPIV	Ridgewood Properties, Inc., WI	Atlanta, GA
SWMC	Stan West Mining Corp.	Scottsdale, AZ
STTX	Steel Technologies, Inc.	Louisville, KY
STKN	Stockton Savings & Loan Association	Stockton, CA
SCAPY	Svenska Cellulosa Aktiebolaget	Sundsvall, Sweden
REGI	Regina Company, Inc. (The)	Rahway, NJ
USBPP	USBANCORP, Inc. (Pfd)	Johnstown, PA
WSTF	Western Financial Corporation	Emporia, KS

NASDAQ/NMS Interim Additions

<u>Symbol*</u>	<u>Name</u>	<u>Date of Entry</u>
AMSB	American Savings Bank, F.S.B.	12/11/85
ARKR	Ark Restaurants Corporation	12/12/85
HLCO	Healthco International, Inc.	12/13/85
METS	Met-Coil Systems Corporation	12/13/85
COGRA	The Colonial Group, Inc. (Cl A)	12/17/85
SITVY	Southbrook International Television Company, plc	12/19/85

The following changes to the list of NASDAQ/NMS securities occurred since December 9, 1985:

NASDAQ/NMS Symbol And/Or Name Changes

<u>New/Old Symbol*</u>	<u>New/Old Security Name</u>	<u>Date of Change</u>
REID/REID	Reid-Rowell, Inc./Reid-Provident Laboratories, Inc.	12/11/85
ABXFF/BRCFF	American Barrick Resources Corp./Barrick Resources Corp.	12/13/85
ERLY/ERLY	Erly Industries, Inc./Early California Industries, Inc.	12/13/85
DKLBB/DKLBB	DEKALB Corporation, (C1 B)/DEKALB AgResearch, Inc. (C1 B)	12/18/85
LAFCA/LAFCI	Loan America Financial Corporation (C1 A)/Loan America Financial Corporation	12/19/85
OJAY/CCSI	Orange Julius International, Inc./ Custom Creamery Systems, Inc.	12/19/85
ALCCV/ALNT	ALC Communications Corporation WI/Allnet Communication Services, Inc.	12/20/85

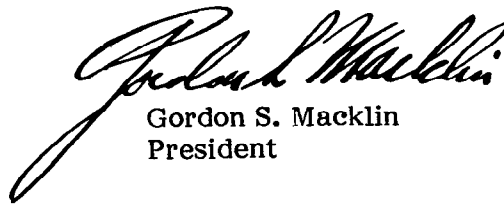
NASDAQ/NMS Deletions

<u>Symbol*</u>	<u>Security Name</u>	<u>Date</u>
FISI	Financial Institution Services, Inc.	12/10/85
FGLFS	Florida Gulf Realty Trust, SBI	12/11/85
CMPQ	Compaq Computer Corporation	12/12/85
ABUG	Spectrum Group, Inc. (The)	12/12/85
ITCP	International Technology Corporation	12/13/85
PTMFQ	PetroMac Energy, Inc.	12/13/85
ITCPW	International Technology Corporation (Wts)	12/17/85
MNAC	Maine National Corporation	12/18/85
SNCO	Second National Corporation	12/18/85

MCFV	McFaddin Ventures, Inc.	12/19/85
NUTR	Nutri-Foods International, Inc.	12/19/85
GOTT	GOTT Corporation	12/23/85
DENLQ	Denelcor, Inc.	12/26/85

Any questions regarding this notice should be directed to Donald Bosc, Assistant Director, NASDAQ Operations, at (202) 728-8043. Questions pertaining to trade reporting rules should be directed to Sharon Belanger, Market Surveillance, at (202) 728-8206.

Sincerely,



Gordon S. Macklin
President

NASD

National Association of Securities Dealers, Inc.
1735 K St., N.W. • Washington, D.C. 20006 • (202) 728-8000

notice to members 85-89

December 31, 1985

TO: All NASD Members

RE: Adoption of New Rule of Fair Practice Relating to Permission for Members to Alter Their Methods of Operation Under SEC Rule 15c3-3 (the "Customer Protection Rule")

The Securities and Exchange Commission has adopted amendments to the NASD Rules of Fair Practice and Code of Procedure which were approved by a membership vote pursuant to Notice to Members 85-43, dated June 12, 1985.

The new rules provide the NASD with an additional regulatory tool in monitoring the financial and operational condition of members that are not designated to another self-regulatory organization for financial responsibility purposes. The new rule provides the NASD with the authority to evaluate, in advance and on a case-by-case basis, a firm's capacity to alter the nature of its business by changing its exempt status under SEC Rule 15c3-3 so as to increase customer financial exposure. The rule is designed to ensure that a member has the necessary capabilities, including adequate net capital and qualified personnel, to conduct the type of business it plans.

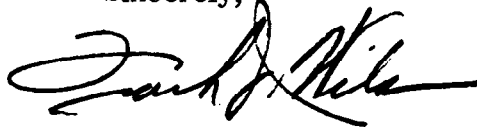
The rule requires an existing member to obtain the NASD's prior written approval before altering its method of operations by changing its exempt status under the Customer Protection Rule. This approval is obtained by submitting a written request to the district office in which the firm is located describing the procedures the member has established to effect an orderly transition of its business. Requirements for approval are contained in new Section 39 of Article III of the Rules of Fair Practice.

Amendments to Article V of the NASD Code of Procedure set forth the time frames for action and the appellate rights of members. In general, the district staff is required to notify a member in writing of its decision to approve or disapprove the change within 15 business days of receipt of the application. If approval is denied by the district staff or if approval is granted with modifications, procedures are provided for a member to appeal that decision to the District Business Conduct Committee, the NASD Board of Governors and, ultimately, to the

Securities and Exchange Commission. A copy of the text of the new rules, which are effective immediately, is enclosed with this notice.

Any comments or questions regarding this notice or the application of the rule should be directed to Thomas R. Cassella, Director, NASD Financial Responsibility, at (202) 728-8237.

Sincerely,

A handwritten signature in black ink, appearing to read "Frank J. Wilson", written in a cursive style.

Frank J. Wilson
Executive Vice President
and General Counsel

Attachment

PROPOSED RULE OF FAIR PRACTICE

Proposed Article III, Section 39 of the Rules of Fair Practice

(a) Application - For the purposes of Article III, Section 39 of the Rules of Fair Practice, the term "member" shall be limited to any member of the Association who is not designated to another self-regulatory organization by the Securities and Exchange Commission for financial responsibility pursuant to Section 17 of the Securities Exchange Act of 1934 and Rule 17d-1 promulgated thereunder.

(b) A member operating pursuant to any exemptive provision as contained in subparagraph (k) of SEC Rule 15c3-3 shall not change its method of doing business in a manner that will change its exemptive status from that governed by subparagraph (k)(1) or (k)(2)(b) to that governed by subparagraph (k)(2)(a); or from subparagraph (k)(1), (k)(2)(a) or (k)(2)(b) to a fully computing firm that is subject to all provisions of SEC Rule 15c3-3; or commence operations that will disqualify it for continued exemption under the SEC Rule 15c3-3 without first having obtained the prior written approval of the Association.

(c) In making the determination to approve, deny or amend an application made pursuant to subsection (b), the Association staff shall consider, among other things, the type of business in which the member is engaged, the training, experience and qualifications of persons associated with the member, the member's procedures for safeguarding customer funds and securities, the member's overall financial and operational condition, and any other information deemed relevant in the particular circumstances for the time these measures would remain in effect.

PROPOSED ADDITION TO THE CODE OF PROCEDURE

Procedures Under Article III, Section 39 of the Rules of Fair Practice

(a) District Staff Procedures

Applications for approval of a change in exemptive status under SEC Rule 15c3-3, required pursuant to Article III, Section 39 of the Rules of Fair Practice, shall be made by filing a written request with the District Office in which the member's principal place of business is located. Such request shall address the criteria set forth in Section 39(c) of Article III of the Rules of Fair Practice. Within fifteen (15) business days of the receipt of such application, the District staff shall make a determination and inform the member, in writing, of its decision to approve, deny or amend the member's request as submitted. If the decision is to deny or amend the member's request in any way, the written decision shall set forth the reasons for such action.

(b) District Business Conduct Committee Review

Whenever a request under subparagraph (b) of Article III, Section 39 of the Rules of Fair Practice is denied in whole or in part by the District staff, the member may, within five (5) business days of receipt of the District's determination letter, petition the District Business Conduct Committee ("DBCC" or "District Committee") for review of such decision. The member will have the opportunity to be heard and to present the reasons why it believes that the decision by the staff should be set aside or modified. Such hearing shall be held before the DBCC or a designated subcommittee thereof within seven (7) business days of receipt of the petition for review. The member shall be entitled to be represented by counsel and a record shall be kept of the proceeding. Thereafter, the District Committee shall, within five (5) business days of the hearing or within five (5) business days of receipt of the member's petition for review if the member waives a hearing and elects to proceed by written petition, issue a written decision affirming, modifying or setting aside the District staff decision and setting forth the reasons for such action. This written decision shall also provide for an appropriate sanction to be immediately imposed for failure to comply with the Committee's determination.

(c) Review by the Board

The written decision issued by the District Committee pursuant to subsection (b) shall be subject to review by the Board of Governors upon application by the mem-

ber filed within five (5) business days of the date of the decision, or the matter may be called for review by the Board on its own motion within thirty (30) calendar days of the District Committee's decision. In the case of an appeal, the member shall be entitled to a hearing before a subcommittee of the Board within fifteen (15) business days. If called for review by the Board on its own motion, the member shall be entitled to a hearing within thirty (30) business days of such call for review. The member shall be entitled to be represented by counsel. Instituting a review, whether by application or on the action of the Board, shall not act as a stay of the action taken by the DBCC unless otherwise ordered by the Board.

(d) Decision of the Board

Upon consideration of the record, the Board of Governors shall, in writing, affirm, modify, reverse or dismiss the decision of the DBCC or remand the matter to the District for further proceedings consistent with its instructions. If a hearing is held, a decision, which shall be the final action of the Board, shall be issued within five (5) business days of the hearing. If no hearing is requested, the matter shall be considered based on the record and a decision shall be issued promptly. In its decision, the Board shall set forth the specific grounds upon which its determination is based and shall provide for an appropriate sanction to be immediately imposed for failure to comply with its directives. Board action restricting the member's activity shall become effective immediately upon issuance of its decision and shall remain in effect until the limitation is removed or modified by the DBCC.

(e) Application to Commission for Review

In any case where a member is aggrieved by an action taken or approved by the Board of Governors, such member may make application for review to the Securities and Exchange Commission in accordance with Section 19 of the Securities Exchange Act of 1934, as amended. There shall be no stay of the Board's action upon appeal to the Commission unless the Commission determines otherwise.