

ALERT

NASD Task Force Takes Hard Look at Regulatory Efforts

The NASD established in April a Regulatory Review Task Force to conduct an indepth review of the NASD's regulation of the over-the-counter market.

At recent meetings, the task force discussed with senior NASD staff the NASD's regulatory procedures, staffing, automation resources, and plans for new products, internationalization, and other changes affecting regulation of the securities business. Senior management also explained how the NASD coordinates its regulatory efforts within the Association and with other self-regulators. Based on staff presentations, committee members are identifying areas for further discussion and possible action.

In response to recent market developments, the NASD has expanded the charter of its Task Force to include the review of a number of structural and quality-of-market issues, including the performance of communications systems, the potential for automated access beyond SOES, dealer capital, competition and dealer obligations, and the impact of international trading. It is expected that a Special Committee of the Task Force will be appointed to undertake this study and to report its findings and recommendations within 120 days of appointment. *(con't. on page 2)*

NASD

TO: All NASD Members

RE: *The Regulatory & Compliance Alert* Newsletter

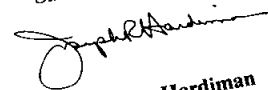
The NASD is pleased to provide members with this inaugural edition of *The Regulatory & Compliance Alert*. Scheduled for publication every two months, *The Regulatory & Compliance Alert* is intended to assist members in avoiding inadvertent and unintentional rule violations by reporting on the latest in regulatory developments, new rules and interpretations, current NASD, SEC, and court decisions, and recently enacted or pending legislation affecting the securities industry.

The newsletter will provide concise summaries of recent disciplinary actions taken by the NASD Market Surveillance and District Business Conduct Committees. In addition, it will direct compliance personnel to areas that require extra attention as well as alert them to other key regulatory developments, issues, and problem areas that may bear directly on members' overall activities.

To encourage dissemination of the information to as many registered persons as possible, the NASD will distribute the newsletter to all main and branch offices of our members.

Any questions about this publication or ideas for making it more useful may be directed to Rob Hessing, Surveillance Department, at (202) 728-8228, or to your local District Office.

Sincerely,



Joseph R. Hardiman
NASD President

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NASD

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Task Force

(con't. from page 1)

The committee will present a preliminary report on its deliberations to the Board of Governors at the January 1988 meeting with the final report expected by March 1988. The committee's report and recommendations will not be limited only to better detection of insider trading, according to Chairman A. A. Sommer, Jr. Instead, they will be truly comprehensive reviews of, and prescriptions for, a much stronger regulatory structure.

The task force chairman is a partner in the law firm of Morgan, Lewis & Bockius. Mr. Sommer is a former SEC Commissioner, former Chairman of the Section on Corporation, Banking and Business Law and of the Federal Regulation of Securities Committee of the American Bar Association, former member of the NASD Board of Governors, and currently General Editor of *Securities Law Techniques*, published by Matthew Bender & Company.

Other members of the task force are:

■ Richard R. West, Dean of the Graduate School of Business Administration of New York University. A former Governor-at-Large of the NASD, he has also served as Chairman and Vice Chairman of the Municipal Securities Rulemaking Board and on the Board of Directors of a number of companies.

■ Irving M. Pollack, lawyer and consultant specializing in legal policy issues relating to capital markets. A former SEC Commissioner and a 33-year veteran of the agency, he held the posts of Director, Division of Enforcement, and Director, Division of Trading and Markets, among others.

■ Russell H. Baumgardner,

attorney, Chairman of Apogee Enterprises, Inc., in Minneapolis. A former Governor-at-Large of the NASD, he is a past president of the Minnesota Association of Commerce and Industry.

■ Stephen L. Hammerman, Executive Vice President, Chief Administrative Officer and General Counsel of Merrill Lynch & Co. A Governor of the NASD, he is a former Assistant U.S. Attorney and a former New York Regional Administrator for the SEC.

■ Allen Weintraub, Senior Executive Vice President and Chief Operating Officer of Advest, Inc., and 1987 Chairman of the NASD's National Business Conduct Committee. He is a former Vice Chairman and Director of the Philadelphia Stock Exchange.

■ Victor Elting, III, Senior Vice President and General Counsel of The Chicago Corporation. A Governor of the NASD, he has served on the Securities Advisory Committee of the Illinois Secretary of State and the Securities Law Committee of the Chicago Bar Association.

■ Richard C. Romano, President of Romano Brothers and Company, and 1987 Vice Chairman of the NASD. He is a former Chairman of the NASD's Chicago District Business Conduct Committee.

■ William R. Rothe, Managing Director of Alex. Brown & Sons, and Chairman of the NASD's Market Surveillance Committee and a member of its Trading Committee.

The senior NASD staff liaison to the task force is Frank J. Wilson, Executive Vice President, Legal and Compliance, who is assisted by NASD Special Counsel Michael J. Kulczak and the NASD Staff Committee on Insider Trading composed of senior

NASD personnel. The members of this committee have broad market surveillance, broker-dealer surveillance, and legal expertise. The committee consists of:

■ James M. Cangiano, Director, Market Surveillance.

■ William S. Clendenin, Vice President, Director, District 12.

■ Dennis C. Hensley, Vice President, Legal.

■ John E. Pinto, Senior Vice President, Compliance.

■ Willis H. Riccio, Vice President, Director, District 13.

■ William R. Schief, Vice President, Regional Attorneys.

Mr. Schief and Mr. Riccio are former SEC Regional Administrators.

As it proceeds with its assignment, the task force will coordinate with other regulatory and self-regulatory bodies in an effort to develop industry-wide solutions to industry-wide problems.

Automated "Pink Sheet" Surveillance Becomes an NASD Priority

The NASD is developing automated systems and programs for more comprehensive, efficient, and effective surveillance of trading in non-NASDAQ over-the-counter securities. The NASD intends to expand its surveillance capabilities and programs to include the estimated 10,000 to 15,000 non-NASDAQ issues listed in the National Quotation Bureau's "pink sheets."

The NASD's Board recently approved a recommendation by a subcommittee of the Market Surveillance Committee to require

members to report price and volume information for trades in non-NASDAQ securities to the NASD on a daily basis. Members would have to electronically transmit this information to the NASD so the Market Surveillance staff could computer capture, retrieve, and analyze it when received.

These developing surveillance programs would also expand NASD field examination procedures to detect unusual trading practices or questionable activities in this market as well as require members to document their best-execution efforts when effecting transactions in "pink sheet" securities.

On the market side, the NASD is actively studying the development of an electronic "bulletin board" with information on these issues.

NASD Takes Steps to Facilitate Access to NASDAQ Market

At its November meeting, the NASD Board of Governors approved for member comment a comprehensive series of proposals for improving computer access to the NASDAQ market and for strengthening the commitment of market makers. Implementation of these proposals will significantly change the rules, mechanics, and operation of the NASD's Small Order Execution System (SOES).

The NASD established its Small Order Execution System to permit execution of small orders in NASDAQ securities efficiently and at the best price for the public

customer. SOES average weekly volume doubled during the week of October 19, 1987. Notwithstanding the extraordinary volume during that and subsequent weeks, SOES remained open and operating and continues to provide investors with an effective means for executing smaller orders.

However, problems did occur. As a result, the NASD Trading and SOES Users Committees concluded that certain improvements should be made to the NASDAQ National Market System (NASDAQ/NMS) market to ensure that investors have access to an even more efficient and liquid market, especially during periods of high volume. The Committees concluded that the most effective way to ensure greater investor access is through enhancements to SOES and the NASDAQ System that will help alleviate the need for firms to rely on telephone contact. Therefore, the Committees recommended certain rule changes to the NASD Board of Governors, who authorized their publication for comment.

In pertinent part, the proposed rule amendments would:

- prohibit a firm that withdraws, on an unexcused basis, as a NASDAQ market maker in a security from re-entering NASDAQ as a market maker in that security for 30 days;

- limit the acceptable reasons for an excused withdrawal from NASDAQ;

- make SOES participation mandatory for all market makers in NASDAQ/NMS securities;

- enable the NASD to establish different levels of maximum order size limits (e.g., 1,000, 500, and 200 shares) for SOES orders, depending on the characteristics of different securities;

- provide that SOES executions will continue in a NASDAQ/NMS security when quotes are locked or crossed, with executions occurring at the best price; and

- eliminate preferencing of market makers during a locked or crossed market situation.

Amendment Details

The proposed amendments would prohibit a firm that withdraws from making a market in a NASDAQ security on an unexcused basis from re-entering as a market maker in that security for 30 days. Currently, market makers may withdraw from and re-enter SOES without penalty and as a NASDAQ market maker after a two-day delay. The Committees and the NASD Board have concluded, however, that it is necessary to impose a penalty on unexcused withdrawals from NASDAQ securities to help ensure that investors in those securities have access to a continuous, liquid market supported by as many market makers as possible.

Market makers will continue to be able to obtain excused withdrawals. However, the conditions under which those withdrawals will be permitted would be limited under the proposal to withdrawals due to physical circumstances (e.g., equipment malfunction or relocation) or legal considerations (e.g., compliance with SEC Rule 10b-6). A market maker obtaining an excused withdrawal could re-enter NASDAQ according to the conditions of the withdrawal (e.g., withdrawals for purposes of equipment relocation would permit market makers to re-enter upon installation at the new location).

The proposals would further require that every market maker in every NASDAQ/NMS

security also be a SOES market maker in that security. SOES participation for market makers in NASDAQ securities that are not NASDAQ/NMS securities would continue to be voluntary. As participants in SOES, all NASDAQ/NMS market makers would be required to clear and settle trades through a registered clearing facility.

This change will facilitate the automatic execution of customers' small orders for every NASDAQ/NMS security without the need for telephone contact between the order-entry and executing firm. Every firm making a market in a NASDAQ/NMS security will be participating in the automatic execution system. By mandating wider participation in SOES, the Committees and the NASD Board believe that the NASD will significantly improve investor access to the NASDAQ/NMS market, particularly in times of high volume.

The SOES rules would be amended to provide that the NASD could establish different maximum order size limits for different securities. As a small-order system, SOES is available for retail agency orders of limited size. The size limits are currently 1,000 shares for NASDAQ/NMS securities and 500 shares for other NASDAQ securities. On the basis of experience, however, the Board has concluded that the efficiency and liquidity of SOES could be improved by refining order size limits so that different categories of securities having certain trading characteristics would be subject to different size limits.

Under this concept, the NASD will study the trading, volume, and price patterns of all NASDAQ/NMS securities to determine appropriate categories of size limits and those securities which should be in each category.

For example, orders in some securities may be restricted to a maximum size of 200 shares, others to 500 shares, and still others to 1,000 shares. Initially, these different tiers will probably apply only for NASDAQ/NMS securities.

The order size limits establish, to a certain extent, the exposure of any SOES market maker to market risk. Because SOES will be mandatory for every NASDAQ/NMS market maker, a firm's willingness to be exposed to SOES executions may be a factor in its decision to be a market maker in NASDAQ/NMS securities.

The SOES rules would be amended to provide that orders in NASDAQ/NMS securities will continue to be executed in a security, notwithstanding that NASDAQ quotations for that security are locked (i.e., at least one market maker is willing to buy for the same price as at least one market maker is willing to sell) or crossed (i.e., at least one market maker is willing to buy at a higher price than another is willing to sell). Under current procedures, SOES orders are executed in rotation against all market makers offering the "inside," or best quotation. However, automatic executions cease if quotations become locked or crossed. An order-entry firm can send an order to the SOES market maker of its choice. This is referred to as "preferencing." If this is done, the order is executed at the best price for that market maker's account even if its quote is not the best. In rapidly changing markets, it is more likely that quotations will be inadvertently locked or crossed as the use of telephones limits access to the market.

Under the proposal, automatic SOES executions in NASDAQ/NMS securities would continue even with locked or

crossed quotes. All executions would be made against the firm causing the locked or crossed situation if its price is the best for the customer. An order-entry firm's indication of a preference for a particular market maker would not be recognized so that no other market maker would be required to execute at another dealer's locked or crossed quote. Although this change may create greater potential exposure for firms whose quotes are locked or crossed, it will help ensure that investors have continuous access to SOES throughout periods of high volume and rapid price movement. The change will also provide an economic incentive for firms to keep their quotations current.

Market-Maker Liability

The proposal contains a specific provision to protect market makers in NASDAQ/NMS issues from open-ended liability and repeated executions in the event they are unable to respond and update their quotes. Under the proposal, after a certain number of executions, market makers would be alerted that they have a period of time to respond and, if they have not done so at the expiration of the period, would be removed from the system as a market maker in that security. SOES currently permits each market maker to set a limit on the number of shares of any security that the system will execute against the firm's account each trading day. Since market making in NASDAQ/NMS securities requires SOES participation, a minimum limit capability will be required in those issues. The current capabilities will continue to be available for non-NASDAQ/NMS issues.

Since withdrawal as a SOES market maker in NASDAQ/

NMS securities on an unexcused basis would now carry a 30-day penalty, the Board concluded that any NASDAQ/NMS market maker subject to automatic removal because its exposure limit has been reached should be given a grace period within which to renew its limit or re-enter a quote. Under the proposal, the grace period would be a standard established by the NASD from time to time depending upon market conditions and other factors. The NASD is continuing to study appropriate ways to address this issue. In any case, should a market maker be unable to respond because of equipment failure, it will be permitted to re-enter when the equipment failure is removed.

Written comments on these issues may be sent to: Mr. Lynn Nellius, Secretary, National Association of Securities Dealers, Inc., 1735 K Street, NW, Washington, DC 20006.

Market Surveillance Committee Suspends, Fines Members, Associated Persons

Members and individuals who violate NASDAQ market rules will find themselves subject to formal disciplinary actions before the Market Surveillance Committee. Composed of executives from securities firms across the country, this committee is responsible for maintaining the integrity of the NASDAQ market and for disciplining NASD members and asso-

ciated persons who fail to comply with market-related securities laws, including transaction execution and reporting, trading practices, and insider trading.

In one case, a former trader for a member firm engaged in "marking the close of the market" in a NASDAQ security owned by the member. By upticking the member firm's quotation in the security within five minutes before the market close on five days, the trader caused the member firm's bid price to be the exclusive high inside bid at the market close on four days and the shared high bid on one day. Before the market opened on each of the following business days, the trader downticked the member firm's quotation in the security below its closing bid of the prior day.

The committee determined that these actions constituted violations of the NASD's anti-fraud provisions under the Rules of Fair Practice by marking the close of the market and entering non-bona fide quotes for the security into the NASDAQ System. As a result the committee imposed a 20-business-day suspension, a \$5,000 fine, and a censure on the trader.

Another "marking the close of the market" case resulted in a \$10,000 fine for the member firm and a \$7,500 fine for its head trader. The committee also suspended the member as a market maker for five business days and the trader for 20 business days. In addition, a second principal received a \$1,500 fine for failure to supervise.

In its decision, the Committee noted that the case involved serious misconduct. "Changing a quotation at or near the close of the market without a bona fide transaction or other reasonable basis creates a false and materially

misleading impression to the investment community that the price movement is the result of normal market forces," the committee said. It also noted concern for "the lack of written procedures and supervision over persons in positions to mark the close of the market. Inadequate supervisory procedures open the door to those tempted to engage in fraudulent activity."

The committee also handles cases involving violations of the NASD's Small Order Execution System (SOES) rules. In one such case, the committee suspended a SOES order-entry participant for 90 days and fined the firm \$10,000. In addition, three principals and two brokers at the firm received fines totaling \$25,000, with the individual fines ranging from \$2,500 to \$7,500.

The committee found that one of the firm's traders repeatedly engaged in order splitting by dividing orders in excess of the 500-share and 1,000-share limits for SOES transactions into smaller parts. This violates the size requirements of SOES. In addition, traders and principals executed numerous SOES transactions for the firm's proprietary trading accounts and for other broker-dealers.

Another case involving SOES violations resulted in a fine totaling \$15,000 against a member and its head trader. In addition, both the member and the trader were censured and the member ordered to adopt and implement supervisory procedures relating to the use of SOES by its associated persons. The actions that led to these sanctions included order splitting, executing proprietary trades through SOES, and failing to establish, maintain, and enforce written procedures for supervising the use of SOES by associated persons.

9 District Business Conduct Committees Take Disciplinary Actions

These cases resulted from DBCC actions which have not been reported to the membership in the monthly updates to the NASD manual or to the media in press releases.

District 2N — San Francisco

The District 2N DBCC censured and fined a northern California member firm and registered principal a total of \$15,000 plus \$500 costs for:

- Not depositing in an escrow account investor funds received in a best-efforts, all-or-none offering.
- Not refunding customer monies when the minimum units had not been sold by the specified termination date.
- Misrepresenting to investors the number of units to be sold in the offering.

The DBCC also censured and fined a member and registered principal in Honolulu, Hawaii, a total of \$10,000 for transferring investors' funds from one limited partnership to two other limited partnerships without the investors' consent. In addition, the respondents failed to disclose to the investors in the first partnership that they had temporarily loaned the investors' funds to the other two partnerships.

In another case, the DBCC imposed a censure and fine of \$3,000 on a registered representative in California for recommending and selling units in a limited partnership to a customer without having reasonable grounds for believing that the recommendation was suitable and providing a falsified customer subscription agreement to the issuer.

The DBCC also filed a complaint against a registered representative and a principal of a member firm in San Francisco alleging violations of Article III, Sections 1, 2, and 27 of the Rules of Fair Practice. The complaint alleges that the member, acting through its representative, effected a series of short-term trades in the account of a customer without reasonable grounds for believing that the transactions were suitable and that the member, through its principal, failed to establish and implement supervisory procedures to detect and prevent the alleged violations.

District 2S — Los Angeles

The DBCC in District 2S filed a complaint against a registered representative in Las Vegas, Nevada, alleging several violations of NASD rules. These include unauthorized transactions, the sale of securities that were neither registered nor exempt from registration in California to a California resident, and the fabrication of a fictitious Nevada address for the California customer to circumvent that state's blue-sky laws.

The DBCC also alleged violations of NASD rules by a San Bernadino, California, member and registered principal. The violations allege that the firm obtained secret profits on transactions with customers by charging both a commission and undisclosed mark-ups and mark-downs on principal transactions. The complaint also charges that the member confirmed these transactions to customers as agent when it had acted as principal for its own account.

District 3 — Denver

The DBCC in Denver penalized a member and registered principal in Denver, Colorado, for charging unfair mark-ups on principal transactions. The NASD firm, whose membership was cancelled for failure to pay fees due the NASD, was censured, ordered to disgorge \$22,000 in profits, fined \$15,000, and, if ever readmitted to membership, prohibited for the first two years from executing any principal transactions. The registered principal was also censured, ordered to disgorge personally \$5,000, fined \$2,500, and suspended from association as principal with any NASD member for six months. In addition, the NASD assessed both respondents costs of \$1,075.

The DBCC also filed a complaint against a registered representative and principal in Prescott, Arizona, for violating Article III, Sections 1, 18, and 33, as well as Appendix E, Sections 19(a) and 27(a) of the Rules of Fair Practice. The complaint alleges excessive trading in the accounts of public customers, misrepresentations of the merits and risks of option trading to induce customers to open options accounts, and failure on the part of the principal to properly supervise the salesman.

District 5 — New Orleans

The District 5 DBCC accepted a letter of Acceptance, Waiver, and Consent with a censure and total fine of \$1,000 from a member and registered principal in Memphis, Tennessee. The violation involves selling investment company shares in a high-yield trust to five public customers

without providing them with the "break points," i.e., reduced sales charges, which are available for larger orders.

District 6 — Dallas

The DBCC in District 6 recently charged a Dallas registered representative with numerous violations of NASD rules. These violations include:

- Converting customer funds for personal use.
- Knowingly submitting false information about a customer's financial condition to the respondent's employing member firm.
- Withdrawing monies from a customer's securities account for personal use.
- Recommending transactions without first determining the suitability of the investment in light of the customer's financial circumstances and objectives.
- Exercising discretion in the account of a customer without obtaining prior written authorization.
- Concealing a customer's statements and confirmations that reflect unauthorized activity by diverting them to personal possession and control.

In another matter, the DBCC accepted a Letter of Acceptance, Waiver, and Consent with a censure and fines totalling \$7,500 from a member and registered principal in Dallas, Texas. The violative activity related to an all-or-none private placement of limited partnership interests. According to the complaint, the respondents failed to promptly transmit investor funds to an escrow account; the escrow agreement failed to provide for the return to investors of subscription funds in the event that all interests were not subscribed by the extended termination date; the respondents withdrew funds from

the escrow account before all interests in the partnership had been sold; the respondents effected transactions while failing to maintain the minimum required net capital under SEC Rule 15c3-1; and the firm's auditor was not independent in accordance with the requirements in SEC Rule 17a-5(f)(3).

District 8 — Chicago

The DBCC in Chicago charged a member firm and two employees in Barrington, Illinois, with a number of registration violations. The charges allege that the member and its personnel failed to file a current and accurate Form BD or amendments; failed to file notices of disciplinary action and/or amendments to individual registrations to reflect complete disciplinary histories; resumed a securities business without proper state registration of either the firm or its personnel; and permitted persons subject to statutory disqualifications to engage in securities activities.

The District 8 DBCC also imposed sanctions on another member firm and two registered principals of the firm for numerous violations of financial responsibility rules. The member and one registered principal were censured and fined a total of \$10,000. The other individual was censured, fined \$25,000, and must get the DBCC's permission to requalify as a financial and operational principal. The infractions included:

- Irregularities in posting margin interest charges owed to the carrying firm with which it maintained its omnibus account.
- Inaccurately calculated the amounts required for deposit in the special reserve account for the exclusive benefit of customers as required under the customer protection rule, Rule 15c3-3.

■ Failure to prepare and maintain weekly reserve formula computations as required by Rule 15c3-3(e)(3) under the Customer Protection Rule.

■ Inaccurately computed net capital and filed inaccurate FOCUS Part I and II Reports with the NASD.

District 10 — District of Columbia

The DBCC in Washington, D.C., accepted a Letter of Acceptance, Waiver, and Consent from a New York-based member that resulted in a censure and fine because its Bethesda, Maryland, branch office used an ad for a public real estate limited partnership that did not conform to SEC Rule 134 and an ad for Government National Mortgage Association certificates that contained misleading statements. In addition to the censure and fine, the branch office must file with the NASD, for a period of one year, all advertisements at least 10 days prior to use.

The DBCC accepted an Offer of Settlement that included a \$1,500 fine from another New York-based member for not timely responding to NASD requests for information made pursuant to Article IV, Section 5 of the Rules of Fair Practice.

District 11 — Philadelphia

The DBCC in Philadelphia alleged registration violations by an associated person at a Philadelphia member firm. The alleged violations include a failure to disclose on the U-4 application a prior conviction for bank embezzlement and the failure to respond to NASD requests for information.

The DBCC also brought a complaint against a Pittsburgh member and registered principal

and a financial principal of the firm for numerous financial responsibility and recordkeeping violations. The causes of complaint include:

- Failing to have and maintain minimum net capital required under the SEC rule.

- Submitting inaccurate FOCUS Parts I and IIA Reports.

- Failing to provide customers with interim financial statements.

- Missing or incomplete entries in the sales blotter, securities-received-and-delivered blotter, and general ledger.

- Inadequate supervision of an employee subject to a membership continuance proceeding.

- Permitting supervision of municipal securities transactions by an unqualified individual.

- Non-disclosure of municipal security call features to customers.

In another case, the Philadelphia DBCC alleged violations by a registered representative that center on a recommendation to a public customer to sell shares in

an option income trust fund and to use the monies to purchase shares of a high-yield fund without first determining the suitability of the recommendation.

District 12 — New York

The DBCC in New York accepted a Letter of Acceptance, Waiver, and Consent and imposed a censure and total fine of \$12,500 on a New York member firm and a registered principal of the firm. The violation involves conducting a securities business while failing to maintain the minimum required net capital.

In a case involving the violation of a restriction agreement, the District 12 DBCC accepted a Letter of Acceptance, Waiver, and Consent with a censure and a \$1,000 fine from a New York member firm. The violation involves the respondent's failure to comply with an agreement to observe limitations imposed by the NASD on the volume of business done by the member in light of prior operational difficulties.

The District accepted a Let-

ter of Acceptance, Waiver, and Consent imposing a censure and a \$7,500 fine on a member firm and registered principal in Jersey City, New Jersey. The complaint stipulates violations that include doing a securities business without the minimum required net capital; failing to prepare a computation of the reserve account before making a withdrawal; failing to deposit and maintain sufficient cash and/or qualified securities in the firm's reserve account; and failing to accurately prepare and maintain certain books and records.

In accepting another Letter of Acceptance, Waiver, and Consent, the DBCC imposed a censure and a \$4,500 fine on a member firm and an employee in New York City. The member, acting through the employee, violated Article III, Section 1 of the Rules of Fair Practice by not using an independent bank escrow agent for three contingent direct participation program offerings as well as releasing investors' funds before the required number of units had been sold.

NASD Automates Routine Examinations

Working together, the NASD's Automation Division and Surveillance Department have developed an Automated Examination System (AES) that combines specialized software with the technology of portable microcomputers, also known as "laptops." The system will help examiners perform reviews of general securities sales practice areas, including mark-ups and mark-downs, best execution, trade reporting, and Rule 10b-10 disclos-

ures. Future enhancements will address the financial and operational portions of routine examinations.

AES will enable examiners to enter trade information into microcomputers directly from the member's records during routine examinations. They can then access inside NASDAQ and CQS quotes and trade reports from the Equity Audit Trail via telephone lines. With AES, examiners will identify apparent sales practice violations, expand their review samples, and gather documenta-

tion prior to leaving the firm, which reduces the need for follow-up visits. AES will also eliminate the need for examiners to prepare handwritten transaction schedules or to look up quotes and trade reports.

"AES marks a major advance in our examination process," says John Pinto, Senior Vice President, Compliance. "It is the first step in bringing automation to the field-inspection process which will permit a broader view of members sales practice activity."