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**An Orientation Program on International
Capital Markets for participants from the
Ministry of Finance,
Securities and Exchange Board of India and
The Stock Exchange, Mumbai.**

**Financial Institutions Reform and
Expansion (FIRE) Project**

November 1996

**Financial Institutions Reform and Expansion (FIRE) Project
US Agency for International Development (USAID/India)
Contract #386-0531-C-00-5010-00
Project #386-0531-3-30069**

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Price Waterhouse



November 30, 1996

Mr. D. R. Mehta
Chairman
Securities and Exchange Board of India
Mittal Court, B Wing
Nariman Point
Mumbai 400 021.

Dear Mr. Mehta,

Re: Orientation program on International Capital Markets for officials of the Ministry of Finance, Securities and Exchange Board of India and The Stock Exchange, Mumbai.

At your request and as a part of our contract with the USAID, Mr. Tom Keyes, Mr. Paul Litteau and Mr. Paritosh Sharma, consultants to Price Waterhouse Capital Markets, developed and conducted an orientation program for officials of the Ministry of Finance, Securities and Exchange Board of India and The Stock Exchange, Mumbai on the U.S. and U.K. Capital Markets. The program included visits to New York, Chicago and London and lasted from October 19, 1996 to October 30, 1996.

Purpose of Activity

The purpose of the visit to New York, Chicago and London was to familiarize the participants of the delegation with the functioning of the international capital markets and provide an opportunity to obtain feedback from the international community- investors, brokers, investment bankers on their perception of the Indian markets. The meetings with various people and organizations were arranged keeping these broad objectives in mind and specifically to expose the participants of the delegation to the concepts of self regulation in the US and UK, Information and models from which to build a regulatory and registration system for the Indian Brokers and Sub-brokers, derivatives trading and regulatory issues in derivatives trading and the changes required in the Indian markets for integration with global markets. The introduction to the participants of the delegation and the topics of their interest were provided to all the organizations visited. These are attached as Attachment A and B. The list of organizations visited and people met is attached as Attachment C.

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Activities Undertaken

Meetings were held with Investment Banking firms with experience in Indian operations to understand their views about the Indian markets and what needs to be done from the policy point of view to expand their exposure to India, and thus develop priorities in the reform of the Capital Markets. Smaller Funds who have not invested in India yet but form a large pool of funds which can be tapped by the Indian markets were also met to understand their view of any constraints that they face. The stock exchanges and the depository and settlement organizations were met both in the USA and UK to understand their operations and regulatory role. Sessions were arranged with the regulators and self regulating organizations in the UK to understand the concept as it has been adopted by the UK and the current debate on strengthening the model.

Sessions were scheduled with Clearing broker dealers to help understand the functioning, duties, risk and exposure, and relative power of various types of broker dealers. Clearing firms in derivatives trading were also met with as was the Chicago Board of Options Exchange, the Chicago Mercantile Exchange and the National Futures Association to understand the derivatives trading operations and the regulatory mechanisms. Meetings were also arranged with firms providing issuer services with emphasis on corporate governance issues.

Findings and Recommendations

Throughout the visit we discussed with the participants the strategy the Indian capital markets should adopt to come up to international standards.

The system change requires a comprehensive plan with a focus on exchanges, brokers, sub brokers, investors, regulators and policy makers and also needs the development of a broad national consensus on structural changes. The program aimed at providing additional information to the participants that will assist such a change.

a. A Comprehensive Strategy for the Indian markets

Throughout the visits to the International investing, broking and investment banking community, emphasis was laid on their perception of the Indian markets and the Indian reform process. It was felt that the International community is observing with interest the process of Indian reforms but are still largely adopting a wait and watch attitude. In relation to the capital markets the need for a clean and convenient settlement system with reduced risks and delays of delivery and registration are topmost among the concerns raised by brokers and investors.

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Concerns were also raised about the awareness among the larger investing community, about the Indian reform process and changes in regulatory environment. It was felt that there is a need to market India Inc. strategically as a precursor to larger and more frequent Indian issues of shares, GDRs and debt internationally and also to increase the flow of foreign capital. There is a need to develop a comprehensive plan for the markets and consensus on the plan needs to be developed among the market participants through seminars and workshops.

b. Corporate Governance issues

The issues of corporate governance and shareholder activism were discussed with various people. The Indian markets are in the middle of a debate on corporate governance and lessons on the roles and responsibilities of institutions can be learned from the experience of the US markets.

c. Best Price Execution for investor, the intermarket trading system

The intermarket trading system in the US was established by a SEC directive which ensures the best price on any exchange to the investor wherever he may place the order. A need for this measure in India which has its basis in investor protection, was clearly identified by the delegation. Though even in the US this initially caused a fall in volume in some exchanges it helped overall liquidity and market confidence to boost the combined volumes for all exchanges. India with its many exchanges needs to have such a system to ensure the best price execution for the investor, wherever he may be located.

d. Settlement, Clearing and Depository operations

Discussions ranged from the history of the depository in the US and UK. Single or multiple depositories were discussed. The investors as users really want convenience at the lowest cost and do not care how the market delivers it, but the opinion among depository professionals was in favor of a single depository or if more than one, they need to establish connectivity with each other to effectively be one.

e. Regulatory structure and self regulation

The role of the SEC and that of the Self regulating organizations, the NASD, NYSE, CSE, CBOE etc was discussed with various market participants and at the meetings with the SEC, NYSE, CSE, CME and the CBOE. The efficacy for having separate regulatory structure for security markets and derivatives markets was discussed. The same was also discussed in the UK with the role of the SIB and

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SFA, NIA, IMRO and LSE as self regulators. The current debate on improving the regulation of the UK markets was useful for the participants as India is in the process of establishing its regulatory model for the markets. The need for an organization to regulate the investor intermediary was stressed by all the participants and the establishment, structure and functions of the NIA were discussed in detail. A similar Self Regulatory Organization for India needs to be considered.

f. Derivatives operations and regulations

The participants visited the Chicago Board of Options Exchange and the Chicago Mercantile Exchange and also the National Futures Association, the Self Regulatory Organization of the Futures Industry in the US. They also visited the Securities and Futures Authority, the securities SRO in the UK. Visits were also made to broker dealer firms dealing in derivatives. The participants felt that the Indian market needs to develop certain market structures before a successful launch of the derivatives markets can be made. All these changes need to be initiated and planned before the launch of the derivatives trading in India.

g. Broker dealer arrangements

The legitimacy of the introducing broker and the independent contractor, the contracts under which all parties function, and the need to keep business flowing through the system all help to balance the power between the parties. The resulting balance allows the retail contact (independent contractor or introducing broker) to be of genuine assistance to their clients in resolving every day problems.

These intermediaries are those most critical to developing investor confidence in the markets and should therefore have sufficient professional expertise to be able to advise their clients. The participants agreed that each Indian market participant must qualify and register within the system. If a Sub broker cannot organize the resources to register as a separate entity, then that Sub broker must register through a registered entity.

h. Securities validity, lending, collateral and broker dealer financing

Securities lending is necessary to the functioning of the options market. The need to build such a mechanism in India was highlighted to participants. An institutional mechanism needs to be created with regulations for providing lending and borrowing of securities and financing of broker dealers.

The need to have a central lost and stolen securities system in India as exists in the

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US was discussed and accepted by the participants as urgent to build credibility.

Next steps

With an exposure to all of the above areas, the policy makers and influencers that formed part of the group would be better placed to create and implement policy for Indian capital market reform. The visit should be followed up with more training and education sessions with the groups from the Ministry of Finance, SEBI and the exchanges, and assistance in specific areas outlined above including:

- Development of an intermarket system for exchange trading so as to be able to provide best price execution for an investor irrespective of his location.
- Introduction of securities lending
- Certification and testing for all capital market intermediaries
- Registration and Regulation of Retail Capital market intermediaries
- Strengthening self regulation through exchanges and other self regulatory organizations
- Developing a central lost and stolen securities system.

For the success of this project the participation and cooperation of your management and staff is essential. We would like to thank you and your colleagues at SEBI for the time, courtesy and cooperation extended to us during the course of this project.

Please get in touch with us at the FIRE project for any clarifications or further information you may require.

Thanking you,

Yours sincerely,

W. Dennis Grubb
Principal Consultant

*An Orientation Program on International Capital Markets
for participants from
Ministry of Finance,
Securities and Exchange Board of India and
The Stock Exchange, Mumbai.*

**United States Agency for International Development (USAID)
Financial Institutions Reform and Expansion (FIRE) Project**

**Price Waterhouse LLP
Mumbai
November 1996**

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 - (3) Constitution and Rules**
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Futures Examination and Branch Manager's
Exam**

J. London Stock Exchange - Listing Requirements

K. U.K. Investors Compensation Scheme

Attachment A.

"Introduction to the Participants" provided to all organizations visited

Attachment A

Participants of the Study Tour from India- An Introduction October 18-31, 1996

Dr. U. Sarat Chandran, *Joint Secretary, Department of Economic Affairs, Ministry of Finance, Government of India*. Dr. Chandran is in charge of the divisions of Capital Markets and External Commercial Borrowing. He has a Ph. D. in Economics from the University of Wisconsin, USA and a Masters in Economics from Williams College, USA.

Mr. Paul Joseph, *Director, Stock Exchange Division, Ministry of Finance, Government of India*. Mr. Joseph has a Masters in Economics and also a M.B.A. with specialization in Finance. He has worked at the Ministry of Finance in a number of positions.

Mr. R. C. Mathur, *Executive Director, The Stock Exchange, Mumbai (Bombay Stock Exchange- BSE)*. The BSE is India's oldest stock exchange. Mr. Mathur is on deputation from the State Bank of India, India's largest bank, where he is at the rank of Deputy Managing Director.

Ms. Anita Kapoor, *Regional Manager, Northern Regional Office, Securities and Exchange Board of India (SEBI)*. SEBI is India's securities market regulator. Before joining SEBI, as an officer of the Indian Revenue Service, Ms. Kapoor worked with the Ministry of Finance at the Central Board of Direct Taxes and the Department of Economic Affairs.

Mr. K. E. C. Raja Kumar, *Regional Manager, Southern Regional Office, Securities and Exchange Board of India*. Before joining SEBI, as an officer of the Indian Revenue Service, Mr. Kumar worked with the Central Board of Direct Taxes, Ministry of Finance in various positions.

Mr. Paritosh Sharma, *Securities Markets Specialist, Price Waterhouse LLP (FIRE Project)*. He has a M.B.A. with specialization in Finance. Prior to joining the project he was General Manager with the OTC Exchange of India, the over the counter market in India. Mr. Sharma is coordinating this study tour.

Attachment B.

"Topics of interest for participants" provided to all organizations visited.

Attachment B

Topics of Interest for Participants

Study Tour from India (New York/ Chicago/ London October 18-31, 1996)

Stock Exchanges

- Exchange Listing Requirements
- The Initial Public Offering process and regulation
- Exchange Trading Systems
- Clearing and Settlement Process; Depository; and Risk Containment
- Capital Adequacy requirements and their monitoring

Investor Protection

- Curbing Market Manipulation and insider trading practices
- Surveillance and Broker audits
- Investor Protection Funds/ Insurance
- Arbitration

Self Regulation

- Historical development
- Role of SROs
- Extent of Regulator Oversight
- Registration of intermediaries and regulatory requirements
- Qualification standards for brokers

Derivatives trading

- The process of trading and settlement
- Risks associated and containment
- Relationship with Cash Markets

Concerns of International Investors

Attachment C.

List of organizations visited and people met.

Attachment C

List of Organizations visited and people met

1. Georgeson and Company Inc.
Mr. John Wilcox, Chairman
Mr. Peter Firestein, Managing Director
Mr. Samir Bahl, Associate Director

2. Bloomberg LP
Mr. Thomas Broderick

3. Morgan Stanley & Co.
Ms. Susan Black, Managing Director
Mr. Vikram Nagrani, Principal
Mr. J.P. Davidson III, Principal
Mr. Robin Roger, Principal
Mr. Charles Vadala, Principal

4. International Portfolio Group
Mr. Michael Burpee, President

5. Depository Trust Company
Mr. Edward McGuire, Secretary

National Securities Clearing Corporation
Ms. Rita O'Sullivan, Vice President, Risk Management
Ms. Margaret L. Koontz, Executive Director, NSCC
Mr. Dennis M. Earle, Managing Director, NSCC

International Securities Clearing Corporation
Ms. Cecilia Humphrey, Manager, International Analysis

International Depository and Clearing Inc.
Mr. Mark Handsman, Executive Vice President
Mr. Richard Myers, President and CEO

6. New York Stock Exchange
Mr. George Ugeux, Executive Vice President, Office of the CEO
Mr. George Sofianos, Director, NYSE
Mr. Robert Mcsweeny, Vice President,
Mr. Aldo J. Martinez, Vice President, NYSE

7. Mesirow Financial Inc.
Mr. Thomas Avgeris, Senior Vice President
Mr. Thomas J. Geary, Vice President
8. Rosenthal Collins LP
Mr. George J. Recchia, Chief Operations Officer
Mr. Robert B. Cihlar, Manager, Sales and Marketing
Mr. Donald Swanson, Sales and Marketing
9. National Futures Association
Ms. Laura Oatney, Director, Public Affairs
Ms. Patricia Chen, Manager, Compliance
Ms. Yvette Christman, Registration Manager
10. Chicago Board of Options Exchange
Dr. William J. Barclay, Vice President, Strategic Planning
Ms. Mary L. Bender, Senior Vice President, Division of Regulatory Affairs
11. Chicago Mercantile Exchange
Mr. Michael Gorham, Vice President, International Market Development
Ms. Colleen Corr, Manager
12. Chicago Stock Exchange
Mr. Stanley Klimek, President, Capital Securities Investment Corporation
Mr. Jim Meyerhoff, Member
13. SEC- Regional Office
14. Foreign and Colonial Emerging Markets Ltd.
Mr. Jeffrey Chowdhry, Director
15. Securities and Investment Board
Mr. John Barrass, Head, International Relations
Ms. Lieslotte Burdorf- Cook, Manager
16. Serious Frauds Office
Mr. George Staple, Director
Mr. R. J. Wardle, Assistant Director
17. Securities and Futures Authority
Mr. David Jones, Public Relations Manager
18. Trio Holdings
Mr. David L. Hagan, Executive Chairman
Mr. Peter R. Minihan, Associate Director, TRIO Equity Derivatives

Mr. David Caplin, Managing Director, Martin Brokers (UK) PLC

19. Goldman Sachs
 - Mr. Carlos Cordeiro, Managing Director
 - Mr. Bim Hundal, Executive Director
 - Ms. Diane A. Petan, Vice President
 - Mr. Zian Naqui, Executive Director

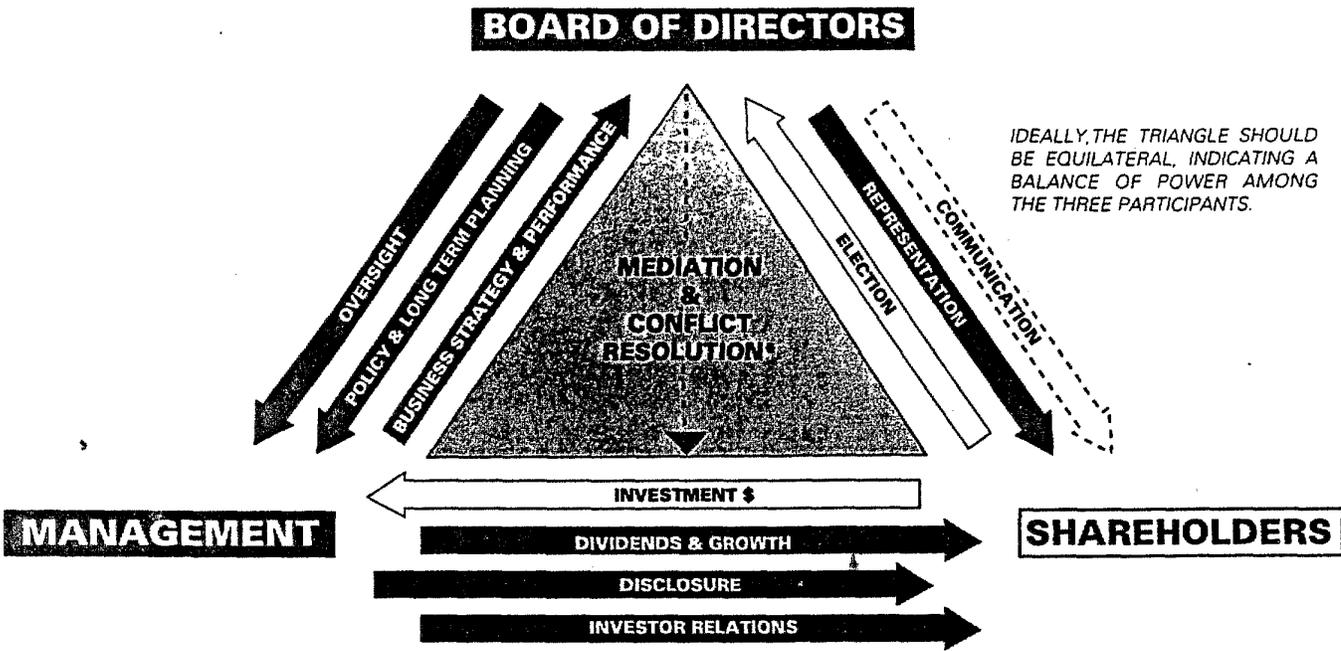
20. Crest Company
 - Ian Saville, Chief Executive
 - Ian Mitchell
 - Paul Symons

21. London Stock Exchange
 - Mr. Ian Salter, Deputy Chairman
 - Ms. Caroline Goodman, Advisor , International Affairs
 - Mr. Alan Wilson, Market Regulation Department
 - Mr. Nigel Atkinson, Head of Listing
 - Mr. David Webb, Regulatory Advisor, Capital Markets
 - Ms. Ramila Patel, Team Manager, Capital Markets

Attachment D.

**Corporate Governance Triangle and article by Mr.
John C. Wilcox, Georgeson & Co.**

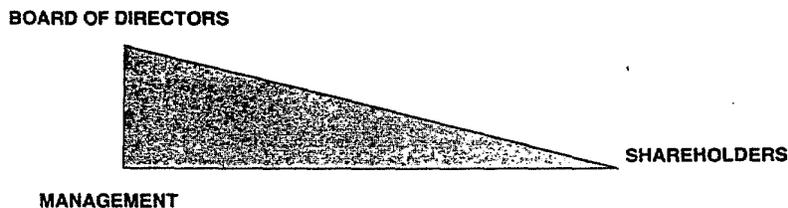
THE CORPORATE GOVERNANCE TRIANGLE



*THE BOARD IS RESPONSIBLE FOR RESOLVING THE STRUCTURAL CONFLICTS THAT ARISE BETWEEN THE CONFLICTING BUT EQUALLY VALID GOALS OF MANAGEMENT AND SHAREHOLDERS ON THE FOLLOWING ISSUES:

- CONTROL
- CAPITAL STRUCTURE
- COMPENSATION OF SENIOR MANAGEMENT
- NOMINATION OF DIRECTORS
- SHAREHOLDER RIGHTS

IN THE U.S. BEFORE TAKEOVERS AND THE RISE OF INSTITUTIONAL ACTIVISM, THE CORPORATE GOVERNANCE TRIANGLE LOOKED LIKE THIS:



INSIGHTS

THE CORPORATE & SECURITIES LAW ADVISOR

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SPECIAL PROXY ISSUE

MAKING THE BEST OF SHAREHOLDER RESOLUTIONS

John C. Wilcox of Georgeson & Company Inc. discusses the expected increase in shareholder proposals during the 1996 proxy season and the steps companies should take when they receive a shareholder resolution.

SHAREHOLDER PROPOSALS

Making the Best of Shareholder Resolutions

Activists are using shareholder proposals, strategically, to highlight concerns about governance and performance. Companies should avoid policy disputes and communicate with shareholders about fundamentals and long-term business strategy.

By John C. Wilcox

All signs indicate that shareholder resolutions will increase substantially during the 1996 proxy season, presenting what many companies view as a no-win dilemma: appeasement, or a public battle for votes against opponents virtually assured of high levels of success. The predictability of institutional votes in favor of policy-based proposals, such as board declassification and poison pill rescission, has created a high level of frustration at targeted companies. They feel victimized by a process that appears to give them no chance of obtaining a hearing on the merits from investors who cast their votes strictly on policy rather than case-by-case.

A Foot in the Door

Confrontation or capitulation are not the only choices available to targeted companies. Often the best choice is to establish communication directly with the proponent in order to determine whether the proposal is negotiable or whether the proponent has another agenda. Shareholder activists are increasingly making strategic use of the proposal process for the purpose of highlighting underlying concerns with governance and performance. In fact, the use of shareholder proposals as a foot in the door—to force a response from companies that ignore other negotiating initiatives—is now more important than the use of proposals as policy instruments.

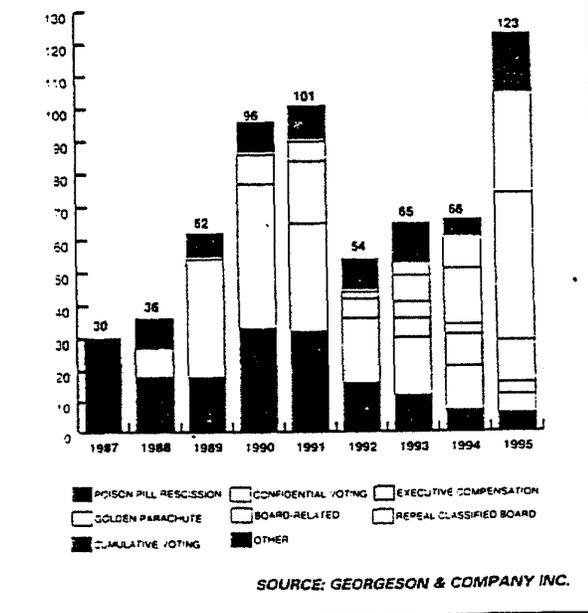
Even the most aggressive shareholder activists are now promoting communication and negotiation rather than confrontation. Bob Monks, a proponent of strategic shareholder activism through his LENS Fund, regards the proposal process as an "invaluable" tool for

shareholders seeking change. He points out that "it almost doesn't matter what the subject of the proposal is," because the process has become so effective in attracting the attention of corporate executives and mobilizing shareholder support.

The Evolution of Strategic Activism

Shareholders took more than five years to perfect this foot-in-the-door strategy. During the early stages of the activist movement—from 1987 through 1992—activists used shareholder proposals as a tool to establish credibility, to enlist support from the Securities and Exchange Commission (SEC) and Congress, and to publicize their agenda of governance reform and shareholder rights. Traditional gadfly tactics were used not just to discredit corporations, but to establish shareholders as a power base. The strategy was undeniably effective and quickly produced a proliferation of new proposals, additional sponsors, and increased institutional voting support (see Figure 1). The peak of success for shareholder activism came in late 1992 when the SEC amended the shareholder com-

FIGURE 1
CORPORATE GOVERNANCE PROPOSALS
SPONSORED BY INSTITUTIONS AND OTHER SHAREHOLDER GROUPS
1987 TO 1995



John C. Wilcox is chairman of Georgeson & Company Inc. in New York, N.Y.

munications rules and adopted new compensation disclosure rules.

A surprising and unanticipated effect of the 1992 amendments was to shift shareholder interest away from Rule 14a-8 resolutions—and from the proxy process in general. By eliminating many regulatory constraints, the new rules freed shareholders to communicate and publicize their views outside the confines of shareholder meetings. This development coincided with the demise of the United Shareholders Association, eliminating a major sponsor of grassroots resolutions. Even more important, the California Public Employees' Retirement System (CalPERS) and other large public pension funds, seeking to justify activism in economic terms, began to investigate and publicize the links between activism, good governance and performance. By 1994, the fraternity of shareholder activists was united behind the belief that "performance" (sometimes referring to operating results, sometimes referring to market return) was the *raison d'être* of activism. The use of shareholder proposals as a blunt instrument to embarrass companies and achieve publicity fell into disuse as performance became the accepted activist goal.

The Renewal of Populist Activism

A new surprise came in 1995 with the near doubling of shareholder proposals, led by the Investor's

Rights Association of America (IRAA), the successor to the United Shareholders Association, and by labor unions (see Figure 2). This new movement appeared to represent a resurgence in gadfly tactics and a partial repudiation of the behind-the-scenes, performance-based strategy that had been developed by large public pension funds. However, IRAA and the unions were careful to piggyback on the established governance agenda in order to enlist voting support from institutional investors. They were thus combining populism, gadfly tactics, and performance-based governance. Both groups centered their campaigns around board-related proposals. IRAA was particularly successful with its campaign against pensions for non-employee directors. Other board-related resolutions included repeal of classified boards, board diversity, a majority of independent directors on boards, and independent directors on nominating committees.

Confrontation or Communication?

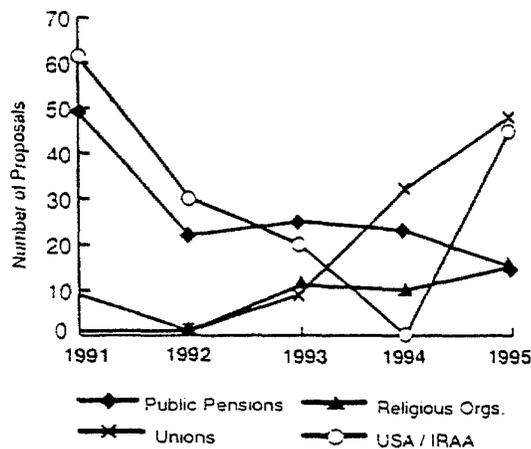
The reappearance of populist activism in 1995 perplexed companies just as they were becoming accustomed to the low-key strategic use of shareholder proposals by public pension funds. It also raised the old tactical question: Do shareholders want confrontation or communication?

The responses from activists willing to discuss their strategies reveal a remarkable uniformity in their assessment of the shareholder proposal process, the importance of communication and negotiation, and even their long-term goals.

Tim Smith, executive director of Interfaith Center on Corporate Responsibility (ICCR), representing primarily religious institutions, says that while his goal is to use the proposal process to change corporate behavior, he views the face-to-face meetings and discussions he holds with companies as far more important than the referendum and voting results. Over the past decade, about one-third of ICCR's proposals have been withdrawn following successful dialogue with targeted companies. Smith believes that corporations are learning how to listen to shareholders. He cites one director of a Fortune 50 company who went so far as to say that shareholder complaints were valuable because they gave his board "early warning" of problems in the company's culture and performance.

Bill Patterson of the Teamster's Union avoids a direct answer to the question most often raised by targeted companies—are unions pursuing a collective bargaining agenda when they sponsor shareholder resolutions? He thinks the question is irrelevant, or at most it

FIGURE 2
CORPORATE GOVERNANCE PROPOSALS
LEVEL OF SHAREHOLDER SPONSORSHIP



SOURCE: GEORGESON & COMPANY INC.

is a question that shareholders can decide for themselves when they vote on union-sponsored proposals. He takes the proxy process at face value and maintains that because government policy encourages both employee ownership and the aggressive exercise of shareholder rights, companies have no choice but to listen to the demands of the growing class of employee-shareholders. Shareholder resolutions are, in his view, an important source of vitality and dynamism in this country's corporate system, which he contrasts with "feudal and fossilized" governance structures in other parts of the world. For 1996, he sees union-sponsored resolutions continuing to focus on board structure and oversight, executive compensation, and poison pills. He agrees that communication is by far the best way for targeted companies to respond to union-sponsored proposals.

Governance and compensation proposals raise fewer strategic concerns and allow greater flexibility in negotiations.

Nell Minow of LENS, Inc. agrees with Patterson that shareholder resolutions are an essential tool to "wake up" managers and directors of poorly performing companies. Her goal is to establish dialogue with targeted companies about how to improve governance practices and performance. Minow believes that corporate culture and management attitudes are inextricably linked to performance, and she maintains that poorly performing companies usually do not like criticism, from inside or outside the company. Conversely, she believes that the best run companies are those that welcome criticism and constantly seek to reinvent themselves. She says that LENS's activism helps companies "scrape off the barnacles" that impede their performance. Like both Smith and Patterson, she advocates private resolution of conflicts rather than public confrontation.

Kayla Gillan of CalPERS and John Lukomnik of New York City Employees' Retirement System (NYCERS) both argue that public pension funds and other indexed, long-term investors are actually the most conservative users of the shareholder proposal process and should be the easiest for companies to deal with. Gillan confirms that CalPERS uses resolutions as a foot in the door with the express goal of starting discussions with the officers and boards of targeted poor performers.

Lukomnik contrasts the relatively benign approach of pension funds with the aggressive tactics of such investors as Kirk Kerkorian, Greenway Partners, LENS,

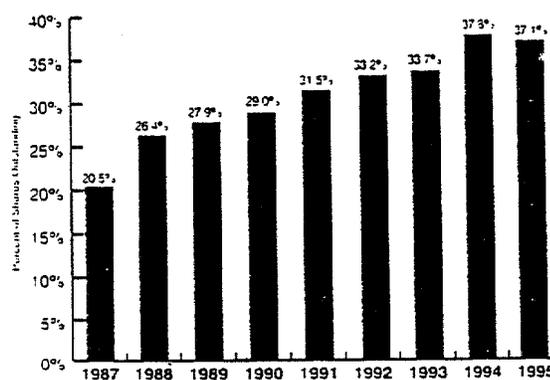
and Michael Price. These investors—heirs to the "raider" traditions of the 1980s—pose far more serious strategic problems for the companies they target.

How Companies Should Respond

Whenever a company receives a shareholder proposal that is not clearly frivolous and that meets the requirements of Rule 14a-8, state law, and the corporate charter, an objective process of evaluation and strategic response should include the following steps.

First, the company should conduct a substantive review of the proposal and the issues it raises. For example, poison pill rescission proposals raise a variety of important policy and strategic questions. (See Figure 3 for the votes on poison pill rescission proposals over the past nine years.) Should the company eliminate the pill? What would be the consequences? Would the proponent be satisfied with lesser modifications, such as a sunset provision, the addition of other "chewability" features, or a promise to modify the pill at a later date? If so, how much would the company increase its vulnerability to a control threat? Are there extraordinary considerations that might persuade shareholders to vote on a case-by-case basis or even to change established voting policies? What additional benefits would accrue from appeasement of the proponent?

FIGURE 3
VOTES FOR PROPOSALS ON POISON PILL RESCISSION
SPONSORED BY INSTITUTIONS AND OTHER SHAREHOLDER GROUPS
1995 ANNUAL MEETING SEASON



SOURCE: GEORGESON & COMPANY INC.

Governance and compensation proposals raise fewer strategic concerns and allow greater flexibility in negotiations. A proponent calling for a separation of the CEO/chairman roles might be satisfied by a move to strengthen the nominating committee's procedures for selecting board nominees or by a clarification of how the CEO's performance is measured. Similarly, a proposal to eliminate certain features of director compensation may be defused by the company's decision to pay directors with stock instead of cash.

Ultimately, it is up to the board to decide what is in the best interest of the company and all shareholders.

Second, the company should analyze its ownership base and calculate the likely outcome if the proposal were put to a vote. The shareholder analysis is similar to other forms of customer research. It identifies who owns the company's stock and analyzes their investment goals, voting practices, and policy preferences. Without this analysis, directors and managers cannot know who they are supposed to represent. A vote projection reveals whether a company's position is strong or weak, what risk it runs in allowing a referendum on the proposal, and how much work would be involved in waging a vigorous campaign against the resolution. These basic marketing and cost/benefit analyses should also take into account the company's recent earnings, overall operating performance, market return, and any other issues, problems, or successes that might affect shareholder attitudes toward the company.

Finally, and most important, the company must bring all these elements together in a communication strategy. If the analyses reveal weak performance, dissatisfied and restless shareholders, and difficult business conditions, the company will likely pursue a

strategy of communication and negotiation aimed at eliminating the proposal and avoiding a potentially embarrassing referendum. Companies with strong performance, facing frivolous proposals or proposals that clash with basic corporate philosophy may decide that communications should be limited and that confrontation is preferable to appeasement.

Conclusion

Companies and shareholders have both come to recognize that shareholder proposals are not an end in themselves, but the means to an end—to establish communications directed at the proper alignment of business and shareholder goals. When proponents assert their desire to be heard and to engage in dialogue with company executives, these assertions should be taken literally. However, communications strategy should always be based on a thorough analysis of the characteristics, goals, and past record of shareholder proponents, as well as on the company's assessment of its own vulnerability and the significance of the proposal. Ultimately, it is up to the board to decide what is in the best interest of the company and all shareholders.

Shareholder activism is now firmly focused on issues of performance. This is good news for companies. It means that negotiations with shareholders about governance and shareholder rights can now be conducted in the context of business fundamentals, operating performance, and market value. Issues such as executive compensation, board structure, and the long list of governance practices are no longer treated as abstract policy questions but are debated in terms of how well a company is doing, how its bottom line can be strengthened, and how its market performance can be improved. These are matters on which companies and shareholders can find common ground, even when they approach the issues from sharply different perspectives.

Attachment E.

Clearing and Settlement in the United States

Clearing and Settlement
IN THE
United States

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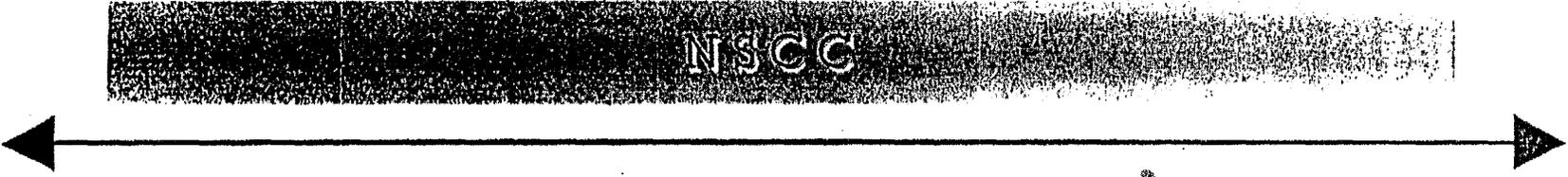
CLEARANCE AND SETTLEMENT IN THE UNITED STATES

SECURITIES	CLEARANCE	SETTLEMENT
Corporate & Municipal	NSCC	DTC
Mutual Funds	NSCC	Mutual Fund or Transfer Agent
Government	GSCC	Fed Reserve
International	IDC/ISCC	Global Clearing Network & Custodians
Mortgage-Backed	MBSCC	PTC or Fed

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same infrastructure

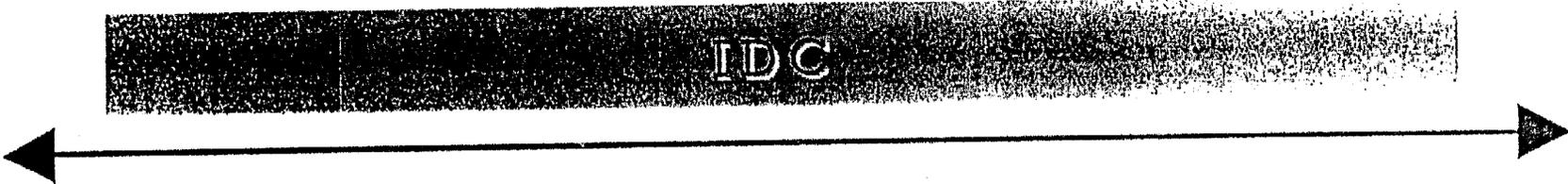
Part of same trust co.



NSCC

- Clearing Services for Equities, Corporate and Municipal Bonds, Mutual Funds, Unit Investment Trusts
- Owned by NYSE, AMEX, NASD
- Guidance From an Independent Industry Board of Directors
- 1,974 Participating Brokers, Dealers, and Banks





IDC

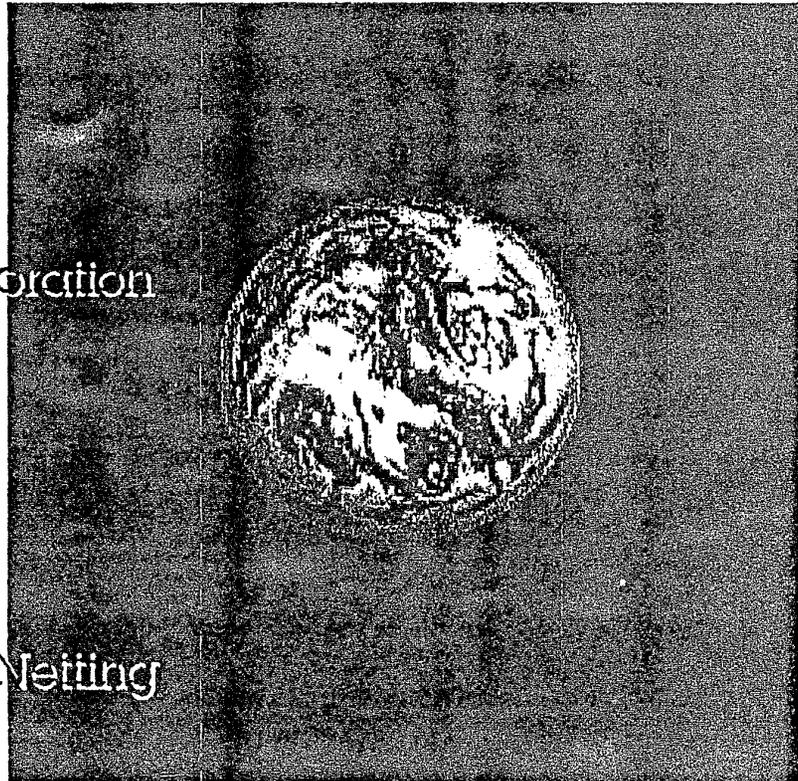
- Joint Venture Between NSCC & DTC
- Provide Integrated Post-trade Processing for International Securities
- Link ID to Various Local and International Settlement Systems



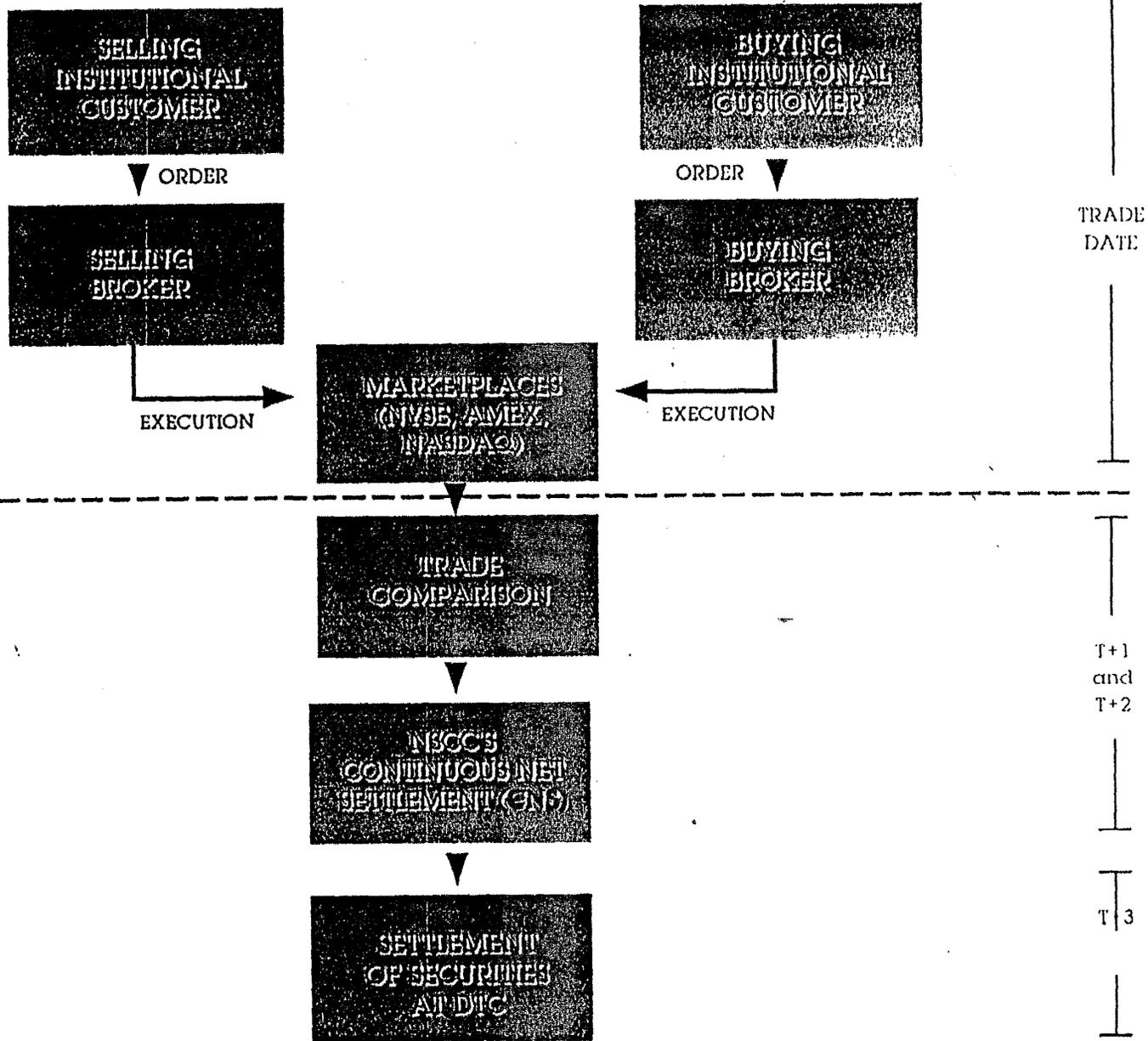
INTERNATIONAL ACTIVITY

■ International Depository & Clearing Inc. (IDC) (Joint Venture with NSCC/DTC)

- International Users of ID
- Global Clearing Network
- Emerging Markets Clearing Corporation
- Central Depository Links
- Standards Initiatives
- Industry Initiatives
- Resource Company
- Foreign Securities Comparison & Netting



TRADE PROCESSING ACTIVITIES - BROKER TO BROKER

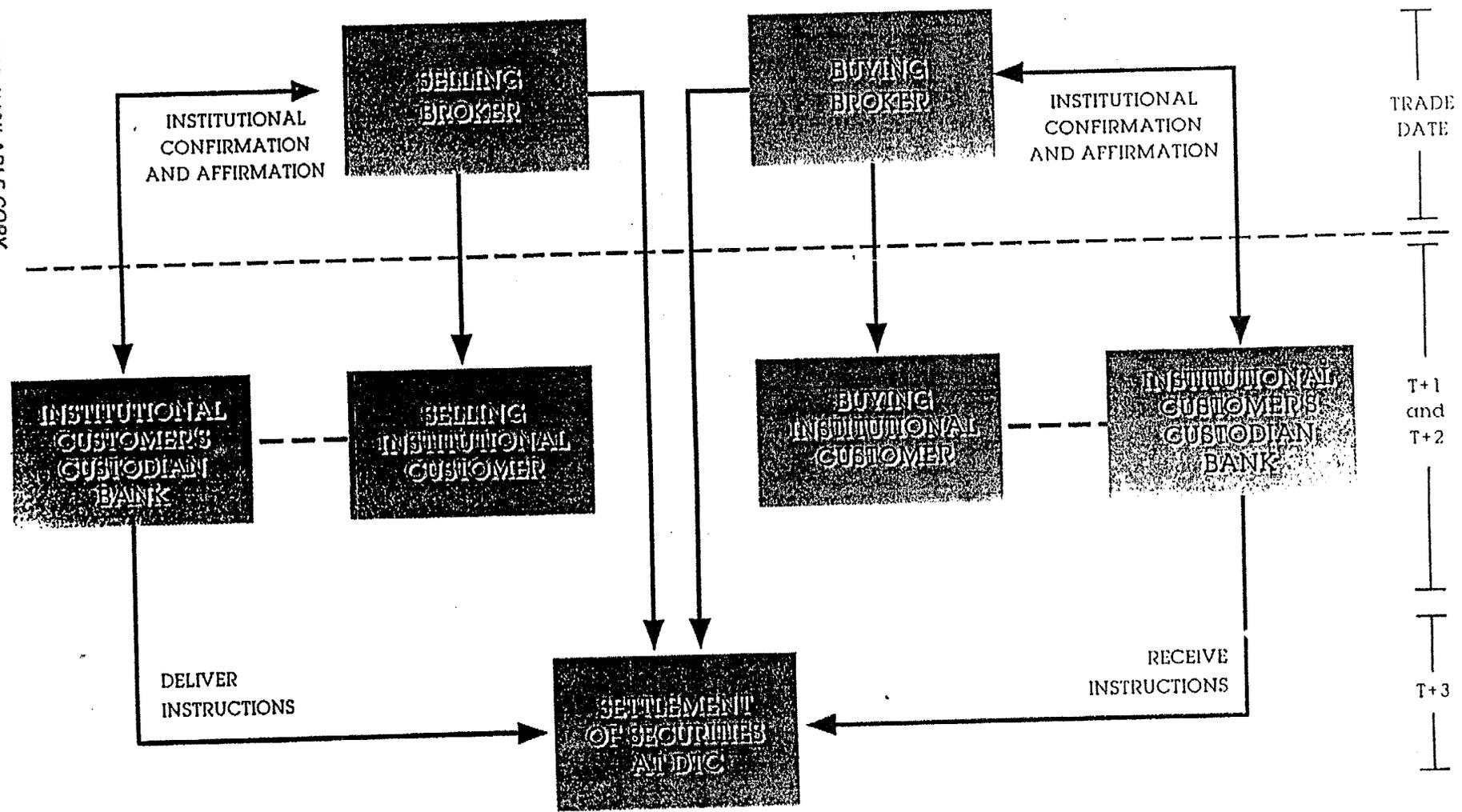


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TRADE-PROCESSING ACTIVITIES - BROKER INSTITUTIONAL CUSTOMER

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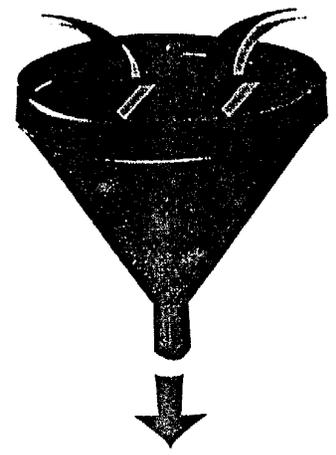


CONTINUOUS NET SETTLEMENT

Net Accounting for Each Participant

By each Security Issue

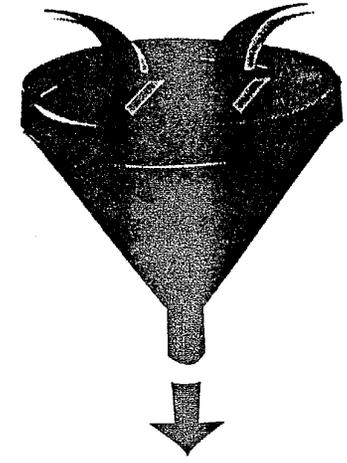
Buys Sells



Net Book-Entry Settlement at DTC

For all cash Credits and Debits

Credits Debits



Net Same-Day Funds Settlement

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34



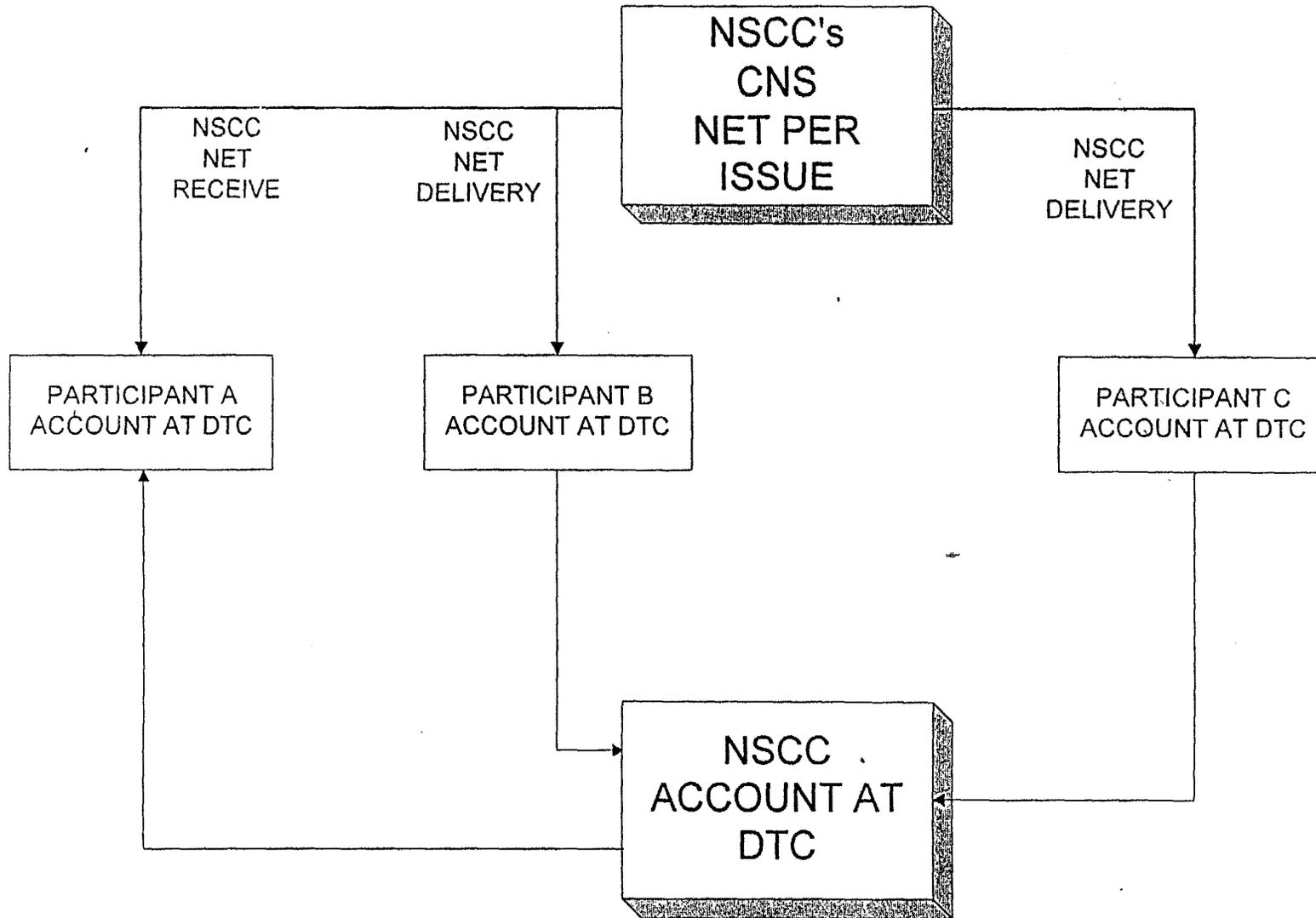
CONTINUOUS NET SETTLEMENT

Benefits:

- Central Fail Control
- Positions Guaranteed
- Dividend and Interest Protection
- Minimizes Number of Deliveries
- Facilitates Automated Processing

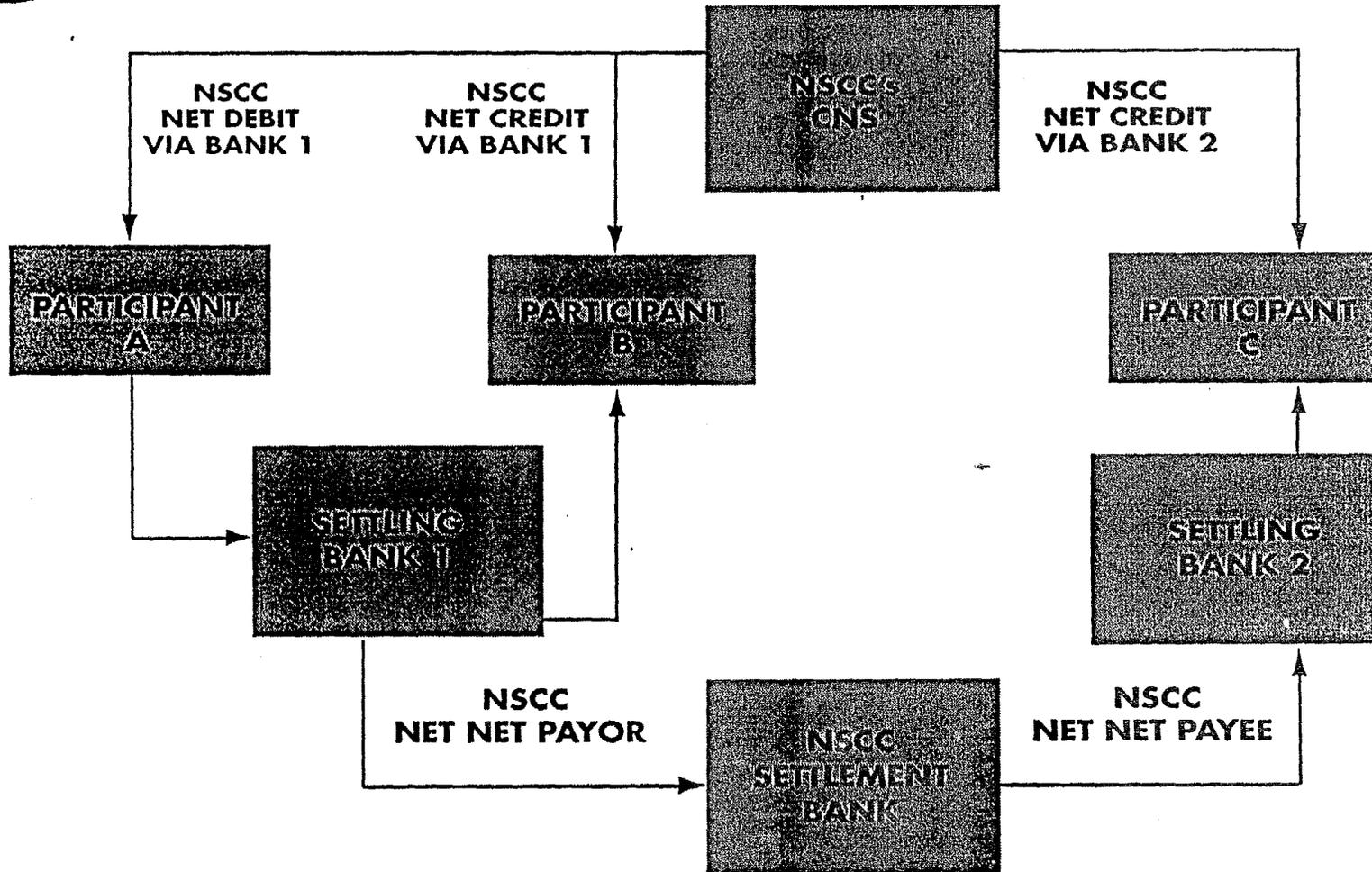
25

SECURITIES SETTLEMENT: BOOK ENTRY AT DTC



of

DAILY NET MONEY SETTLEMENT: NSCC SAME-DAY FUNDS SYSTEM



AUTOMATED CLEARANCE

- Trades transmitted to NSCC
 - Participants
 - Automated marketplace trading systems
- Continuous Net Settlement (CNS) reduces security movements
- Book-Entry delivery (DTC)
- Securities held at depository (DTC)

Attachment F.

National Securities Clearing Corporation-

- (1) NSCC Risk Measurement and Risk Management
by Rita O'Sullivan, Vice President, Risk
Management**
- (2) Standards of Financial Responsibility**
- (3) Brochure**
- (4) Stock Borrow Program**

NSCC RISK MEASUREMENT AND RISK MANAGEMENT
Rita O'Sullivan, Vice-President, Risk Management: Assessments

❖ **THE NATURE OF 'RISK' - how to measure and manage**

❖ **BUSINESS RISK: Uncertainty**

- ◆ Future value of the firm: financial risk analysis
- ◆ Exposure to the clearing corporation from a Member's insolvency
 - orderly wind down
 - sufficient collateral
 - expected and unexpected insolvencies

❖ **SOURCES OF BUSINESS RISK**

- ◆ Credit Risk/Counter Party Risk
- ◆ Liquidity/ Funding Risk
- ◆ Market Risk
- ◆ Legal and Fiduciary Risk
- ◆ Operational Risk
- ◆ Event Risk

❖ **CREDIT RISK/COUNTER PARTY RISK**

NSCC Guarantee

- encourages greater **liquidity in the market**
- easier to **raise capital** / reduces cost of capital raising
- best prices for customers

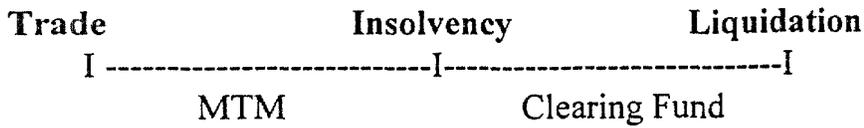
Legal Structure

- clear right to **collateral - priority**
- unfettered **rights to close out positions** if insolvent

❖ **LIQUIDITY/FUNDING RISK**

meet payment for all deliveries where member is insolvent and cannot receive securities - use total aggregate Clearing Fund

❖ **Market Risk**



❖ **MEASUREMENT**

◆ **Management Reports/ NSCC Surveillance Department**

- ▶ extensive array of detailed reports
- ▶ covers all aspects of Member activity
- ▶ automatically generated each day
- ▶ monitored to track Members' activity and exposure

◆ **Financial Reports**

- ▶ outline financial position of the Members
- ▶ produced monthly or quarterly

◆ **NSCC Risk Assessment**

- ▶ reviews NSCC's risk exposure and the adequacy of its risk protection factors

◆ **News / Industry/ Other DEA information Monitoring**

- ▶ NSCC Surveillance Department daily monitoring

❖ **RISK PROTECTION FACTORS**

◆ **Netting System Protections**

◆ **Members' Financial Soundness**

◆ **Clearing Fund**

❖ **SUFFICIENT COLLATERAL**

- ◆ Large \$ value positions - concentration of positions
- ◆ Liquid / Illiquid Securities

“Concentration”

Positions both size of \$ and volume

“Liquid Securities”

MTM and Volatility

“Illiquid Securities”

- market domination: trading large positions
holding large positions

“Bear raid and short squeeze” scenarios

- market price
- players in the market
- which market is affected

❖ **RISK MANAGEMENT SYSTEMS**

- developed in-house
- shared with other entities

❖ **NSCC RULES AND PROCEDURES**

Clearing Fund requirements and Special collateral - ongoing development of new procedures

Rita A. O'Sullivan

NSCC Vice President, Risk Management: Assessments

Ms O'Sullivan joined the National Securities Clearing Corporation (NSCC) in January 1995. Ms O'Sullivan is responsible for conducting risk assessments for NSCC, the Government Securities Clearing Corporation, and the Mortgage Backed Securities Clearing Corporation, including reviewing the services and guarantees provided, evaluating possible risk exposure, and determining and implementing effective protective devices and recovery capabilities.

Prior to joining NSCC, Ms O'Sullivan was the Manager and General Counsel of the Securities Exchanges Guarantee Corporation Limited (SEGC) in Sydney, Australia. SEGC is a subsidiary of the Australian Stock Exchange Ltd and it administers the investor protection scheme for investors and brokers in the securities industry. She also performed risk assessments for SEGC arising from the expansion of ASX's operations, including the development of its futures and derivatives markets, and the expansion of brokers' businesses.

Ms O'Sullivan received Bachelor degrees in the Arts, Laws, and Economics from the University of Queensland, Australia and a Graduate Diploma in Applied Finance and Investment from the Securities Institute of Australia. Ms O'Sullivan has practised as a Commercial Lawyer in Australia and Papua New Guinea, and has worked in the policy area of the Companies and Securities Branch at the Australian Federal Attorney-General's Department dealing with financial sector issues including the oversight of stock and futures exchanges, the responsibility for legislation involving the securities and futures industries, company mergers, acquisitions and takeovers, the licensing of participants, clearance and settlement systems and insider trading.

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ADDENDUM B

STANDARDS OF FINANCIAL RESPONSIBILITY
OPERATIONAL CAPABILITY

The Corporation shall apply the following standards in determining the financial responsibility and operational capability of Settling Members and applicants for membership and shall follow the Guidelines in making surveillance determinations.

I. MEMBERSHIP STANDARDS

- A. In addition to the requirements established pursuant to the provisions of Rule 2, an applicant for membership shall:
1. have sufficient financial ability to make anticipated contributions to the Clearing Fund and to meet obligations to the Corporation; and
 2. have an established business history of a minimum of six months or personnel with sufficient operational background and experience to ensure the ability of the firm to conduct such a business; and
 3. have adequate personnel capable of handling transactions with the Corporation and adequate physical facilities, books and records and procedures to fulfill anticipated commitments to and to meet the operational requirements of the Corporation and other Settling Members with necessary promptness and accuracy and to conform to any condition and requirement which the Corporation reasonably deems necessary for its protection or that of its Settling Members; and
 4. not be known to be subject to a Statutory Disqualification or an order of similar effect issued by a Federal banking agency; and
 5. not be known to be subject to any other action or condition the existence of which would require the applicant to be placed on surveillance by the Corporation.
- B. In addition to the foregoing standards,
1. All broker/dealer applicants shall:

(ADDENDUM B - 2)

- a. have \$50,000 in excess net capital over the minimum net capital requirement imposed by the SEC or such higher minimum capital requirement imposed by the brokers/ dealer's designated examining authority; and
- b. have a capital ratio or percentage that would not require the applicant to be placed on immediate surveillance by the Corporation; and
- c. not be known to be on a "closer-than-normal" surveillance by the applicant's designated examining authority as that term is defined by the applicant's designated examining authority.

2. Bank applicants, other than applicants for Settling Bank Only Membership shall:

- a. (i) have at least \$50 million in capital;¹ or
 - (ii) have furnished to the Corporation a guarantee of its parent bank holding company respecting the payment of any and all obligations of the bank applicant, and such parent bank holding company shall have total consolidated capital of at least \$50 million; or
 - (iii) in the case of a trust company that is not a bank, but is a member of the Federal Reserve System or is an institution insured under the Federal Deposit Insurance Act, have consolidated capital of at least \$10 million and that is adequate in the judgment of the Corporation to the scope and character of the business conducted by such trust company; and
- b. not be operating at a loss at the time of its application and not have operated at a loss in any of its previous three fiscal quarters.

3. Municipal Securities Brokers' Broker sponsored account applicants who elect the Alternative Clearing Fund Formula, in addition to the requirements imposed by Section I.B.1 above, shall:

- a. be in compliance with SEC Rule 15c3-1(a)(8); and,

¹ For the purpose of the membership standards and surveillance status rules applicable to banks. "capital" is defined to include capital stock, surplus, undivided net profits, reserve for contingencies and other capital reserves.

b. sign and deliver to the Corporation an agreement in writing whereby the applicant shall agree that

(i) if securities received on a business day are pledged prior to money settlement on that business day, the Corporation shall be paid directly by the pledgee bank the amount the applicant is required to pay for the securities received or the applicant's net settlement obligation for that business day whichever is less; and

(ii) no securities received on a business day through a qualified securities depository shall be placed in transfer, withdrawn or delivered to a third party for no value prior to paying the Corporation the amount the applicant is obligated to pay for the receipt of the securities or the applicant's net settlement obligation for that business day whichever is less.

4. All applicants for membership limited to the use of the Mutual Fund Services shall meet the following:

a. If a broker-dealer:

(i) has \$25,000 in excess net capital over the minimum net capital requirement imposed by the SEC or such higher minimum capital requirement imposed by the broker/dealer's designated examining authority, and,

(ii) the standards in (i) (B) (1) (b) and (c) set forth above.

b. If a Bank or Trust Company:

(i) has \$100,000 minimum excess capital over the capital requirement imposed by its state or federal regulatory authority, and,

(ii) the standard set forth in (i) (B) (2) (b) above.

5. All other applicants shall be required to meet financial stability standards as are applied to the industry in which the applicant is associated.

C. Unless the context otherwise requires, the parent bank holding company of a Settling Member that has been admitted to membership in accordance with section (i)(B)(2)(a)(ii) of the standards, and any material banking subsidiary of such parent bank holding company, shall, for the purpose of applying the

(ADDENDUM B - 4)

surveillance status rules, be treated as if it were also a Settling Member, so that the Settling Member, the parent bank holding company, and any affiliated material banking subsidiary will be required individually to meet the standards for a Settling Member not under surveillance, if the Settling Member is not to be placed on a surveillance status.

- D. A Settling Member who is placed on "Advisory" surveillance status, shall be required to make any additional Clearing Fund deposits within ten (10) business days of receipt of the Corporation's request.
- E. A Settling Member who is placed on Class "A" or "B" surveillance status shall be required to make any additional Clearing Fund deposits within such time period as the Corporation may require but in no event shall such time period be less than two (2) business days.
- F. A Settling Member who is (i) placed on any surveillance status, or (ii) has a position in a security which is placed on surveillance status, and who is required to make additional security mark-to-the-market payments, in amounts to be determined by the Corporation, shall make such payments within such time period as the Corporation may require but in no event shall such time period be less than two (2) business days.
- G. Settling Members who are required to provide information pursuant to the provisions of Rule 15 shall, except for FOCUS Reports for which the time frame has been prescribed and unless the Corporation deems that a longer period is appropriate, provide such information within two (2) business days, provided, however, that if such information is necessary for a determination in a summary action proceeding it shall be produced immediately.
- H. Bank and Trust Company Settling Members shall be required to file the following information (Settling Members admitted pursuant to section (i)(B)(2)(a)(ii) shall be required to submit information for the Settling Member, its parent bank holding company and any affiliated material banking subsidiary of such parent bank holding company) and any information filed with the Corporation shall be held confidential to the same extent as is provided with respect to information furnished under Section 2 of Rule 15:

INFORMATION TO BE FILED MONTHLY

1. Whether a Federal banking agency has served the Settling Member with a temporary cease and desist order pursuant to Section 8 (c) of the Federal

Deposit Insurance Act regarding any violation of law, rule or regulation or any unsafe or unsound practice which could cause insolvency or substantial dissipation of assets or earnings of the Settling Member or is likely to seriously weaken the condition of the Settling Member or otherwise seriously prejudice the interests of depositors or which could otherwise affect the financial condition of the Settling Member;

- a. indicate the nature of the violation and whether such violation could affect the Settling Member's financial or operational ability to continue to fulfill its obligations to the Corporation;
2. whether the Settling Member has been instructed by the Securities and Exchange Commission or by a Federal banking agency to reduce or eliminate some or all of its clearing activity;
 - a. indicate what type of activity has been restricted and the extent to which it has been restricted;
 3. whether the Settling Member is prohibited from paying dividends or would be required to obtain consent of a bank regulatory authority if it were to pay dividends in an amount equal to 50% of the average amount paid in the past two years;
 - a. indicate the applicable restriction;
 4. whether the Settling Member has sought or received financial assistance from the Federal Deposit Insurance Corporation pursuant to section 13(c) or (e) of the Federal Deposit Insurance Act;
 5. whether a director or officer of the Settling Member was served by a Federal banking agency with a written notice of intent to remove such person from office pursuant to section 8(e)1 or 8(e)2 of the Federal Deposit Insurance Act;
 6. whether the Settling Member was assessed any penalty pursuant to section 8(i) of the Federal Deposit Insurance Act for any violation of any cease and desist order issued by a Federal banking agency or any consent agreement entered into with a Federal banking agency regarding a violation of a law, rule or regulation or any unsafe or unsound practice, which might materially affect the Settling Member's financial condition;

(ADDENDUM B - 6)

- a. indicate whether such penalty brings into question the continued financial or operational capability of the Settling Member to continue to fulfill its obligations to the Corporation;
7. whether the Federal Deposit Insurance Corporation has served the Settling Member with written notice of intent to terminate the Settling Member's federal deposit insurance pursuant to section 8(a) of the Federal Deposit Insurance Act;
8. whether the Settling Member has received extended credit from the Federal Reserve discount window other than seasonal credit;
9. if the Settling Member or its parent bank holding company maintains Moody's or Standard & Poor's bond or commercial paper rating, whether such rating has changed or been withdrawn;
 - a. indicate the effective date on which the rating has changed or been withdrawn;
 - b. indicate old rating and new rating;
10. whether the Settling Member or any of its employees is subject to a statutory disqualification as defined by the Securities Exchange Act of 1934, as amended or is subject to an order of similar effect issued by a Federal banking agency;
11. whether the Settling Member has had a decline in capital since the time it was admitted to the Corporation;
 - a. explain any extraordinary circumstances that account for the decline in capital;
12. whether a Federal banking agency has served the Settling Member with a permanent cease and desist order pursuant to Section 8(b) of the Federal Deposit Insurance Act regarding any violation of a law, rule or regulation or any unsafe or unsound practice, other than a violation of the consumer lending laws which, in the opinion of the Settling Member, could not have a material negative effect on the Settling Member's financial condition;

- a. indicate the nature of the violation and whether such violation could affect the Settling Member's financial or operational ability to continue to fulfill its obligations to the Corporation.

INFORMATION TO BE FILED QUARTERLY

1. Whether the Settling Member has had a material increase or change in volume or in the nature of business which involves additional use of the Corporation's services without corresponding increases in profitability or additions to capital over a period of three or more months;
2. whether the Settling Member has incurred net losses in the fiscal quarter exceeding 10% of its capital.

INFORMATION TO BE FILED ANNUALLY

1. Whether the Settling Member had a consolidated net loss in the fiscal year just ended;
 2. whether the Settling Member has incurred a decline in consolidated net income (after securities gains and losses) in the fiscal year just ended or in the last two fiscal years, amounting to more than 50% of such consolidated net income for the preceding fiscal year;
 - a. indicate whether the Settling Member or its parent bank holding company maintains a Moody's or Standard & Poor's bond rating of at least A, or commercial paper rating of at least P2 or A2;
 - b. indicate whether the Settling Member's capital is 5% or more of its total assets at the end of fiscal year just ended;
 3. whether the Settling Member had net losses in the fiscal year just ended exceeding 10% of the Settling Member's capital.
- I. All broker/dealer Settling Members, except Fund/Serv Broker-Dealers, shall be required to file the following information annually, within such time period as the Corporation shall prescribe, and any information filed shall be held confidential to the same extent as is provided with respect to information furnished under Section 2 of Rule 15:

NAME OF MEMBER _____

ADDRESS OF MAIN OFFICE _____

I. BACKGROUND INFORMATION

1. Form of Organization

Corporation _____
Partnership _____
Sole Proprietorship _____

2. Date Business Started _____

3. Designated Examining Authority _____

4. Exchange Memberships _____

5. Other Memberships _____

6. Briefly describe any recent membership changes as well as those contemplated during the next six (6) months.

7. Chief Executive Officer _____

8. Financial Officer _____

9. Operational Officer _____

10. Number of registered representatives _____

11. Number of operational personnel _____

12. Number of branch offices and state(s) located _____

13. Name of outside counsel _____

14. Name of accounting firm _____

15. Date of last annual outside audit _____

16. Date of last inspection by Designated Examining Authority

17. Is SEC Registration currently effective? Yes ___ No ___

If yes, on what date? _____

18. Method of Record keeping

Manual _____
Computer _____ (in-house)
Other _____

19. If a Service Bureau is to be used, give name and address:

20. Location of books and records if other than Main Office

21. If Member is affiliated with, controls, and/or is controlled by any another business entity, describe details of relationship.

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22. List all banking relationships and available lines of credit.

23. Clearing Arrangements:

OTC:

Self-Clearing Yes No

Through Others

List Names:

For Others

List Names:

Listed:

Through Others

List Names:

For Others

53

List Names:

Options:

Through Others []

List Names:

For Others []

List Names:

Briefly describe any changes contemplated in the Member's clearing arrangement.

II. TYPE OF BUSINESS CONDUCTED

1.(a). Check, in appropriate box, types of business engaged in (or to be engaged in, if not yet active) by Member. Do not check any category which account for or is expected to account for less than 10% of annual gross revenue from the securities or investment advisory business.

[] Exchange member engaged in exchange commission business.

[] Exchange member engaged in floor activities.

[] Broker or dealer making inter-dealer markets in corporate securities over the-counter.

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(ADDENDUM B - 12)

- Broker or dealer retailing corporate securities over-the-counter.
- Underwriter or selling group participant (corporate securities other than mutual funds).
- Mutual fund underwriter or sponsor.
- Mutual fund retailer.
- U. S. Government securities dealer.
- Municipal securities dealer.
- Municipal securities broker.
- Broker or dealer selling variable life insurance or annuities.
- Solicitor of savings and loan accounts.
- Real estate syndicator.
- Broker or dealer selling oil and gas interests.
- Put and call broker or dealer option writer.
- Broker or dealer selling securities of only one issuer or associated issuers (other than mutual funds).
- Broker or dealer selling securities of non-profit organizations (e.g., churches, hospitals).
- Investment advisory services.
- Broker or dealer selling tax shelters or limited partnerships.
- Stock borrowed.
- Other (give details).

(b) Does Member effect transactions in commodity futures, commodities or commodity options as a broker for others or dealer for its own account?

Yes _____ No _____

(c) Does Member engage in any other non-securities business? (If "Yes", describe each such other business briefly.)

Yes _____ No _____

2.(a). Record three (3) primary sources of Member's income during most recent twelve (12) month period.

_____ %
_____ %
_____ %

(b) Projected changes:

3. Securities accounts for customers:

Approximate number of active accounts.

Cash _____
Margin _____

Clientele

56

Retail _____
Institutional _____
Wholesale _____

Types of Accounts

Discretionary _____
Investment Advisory _____
Other (Specify) _____

Services:

Safekeeping [] Proxy [] Research []

Accommodation Transfers []

Other (specify) _____

4. Approximate number of monthly tickets _____

5. Market Making Activities

Does Member make markets? Yes ____ No ____

OTC # _____ Listed # _____

Approximate number of markets to be made on NASDAQ _____, off
NASDAQ _____.

Price range of securities _____

Wire connections _____

Does Member act as correspondent for another broker-dealer?

Yes ____ No ____

If yes, for whom? _____

Does another broker-dealer act as correspondent for Member?

Yes ____ No ____

If yes, who? _____

51

List any current correspondent relationships.

Number currently in registration _____

Number in process of registration _____

Number completed within last twelve (12) months as a sole underwriter

Number completed within last twelve (12) months as a selling group member

Average offering price of those in registration _____

Average offering price of underwriting completed _____

7. Briefly describe any changes contemplated during next six (6) months in the Member's business activities.

III. BONDING

Is Member required to have a fidelity bond?

Yes [] No []

Name of insurance company:

Fidelity \$ _____
On Premises \$ _____

(ADDENDUM B - 16)

In Transit	\$ _____
Misplacement	\$ _____
Forgery and Alteration	\$ _____
Securities Loss	\$ _____
Fraudulent Trading	\$ _____
Amount of Deduction Provision	\$ _____

Expiration date of bond: Mth: _____ Day: _____ Yr: _____

Is there a cancellation rider? Yes _____ No _____

Briefly describe any claims paid.

Briefly describe any changes contemplated in Member's bonding coverage.

IV. PENDING INVESTIGATION(S) AND/OR LITIGATION(S)

Is the Member the subject of any investigation(s), hearing(s), injunction(s), operational restriction(s) or other actions by a regulatory body?

Yes _____ No _____

Is the Member currently involved in any litigation of a criminal or civil nature?

Yes _____ No _____

DATE: _____ SIGNATURE: _____

- J. All Fund/Serv Broker-Dealers shall be required to file the following information annually, within such time period as the Corporation shall prescribe, and any information filed shall be held confidential to the same extent as is provided with respect to information furnished under Section 2 of Rule 15:

NAME OF MEMBER _____

ADDRESS OF MAIN OFFICE _____

I. BACKGROUND INFORMATION

1. Form of Organization

Corporation _____
Partnership _____
Sole Proprietorship _____

2. Date Business Started _____

3. Designated Examining Authority _____

4. Exchange Memberships _____

5. Other Memberships _____

6. Briefly describe any recent membership changes as well as those contemplated during the next six (6) months.

7. Chief Executive Officer _____

8. Financial Officer _____

(ADDENDUM B - 18)

9. Operational Officer _____

10. Number of registered representatives _____

11. Number of operational personnel _____

12. Number of branch offices and states(s) located ____

13. Name of outside counsel _____

14. Name of accounting firm _____

15. Date of last annual outside audit _____

16. Date of last inspection by Designated Examining Authority _____

17. Is SEC Registration currently effective?

Yes ___ No ___

If yes, on what date? _____

18. Method of Record keeping

Manual _____

Computer _____ (In House)

Other _____

19. If a Service Bureau is to be used, give name and address:

20. Location of books and records if other than Main Office

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21. If Member is affiliated with, controls, and/or is controlled by any other business entity, describe details of relationship.

22. Does Member engage in any non-Mutual Fund business? (If "Yes", describe each such other business briefly.)

Yes _____ No _____

II. NATURE OF BUSINESS

1. With what Mutual Funds does Member conduct business?

2. What is the largest daily money settlement Member anticipates having with any one Mutual Fund Group?

Less than \$100,000 []
Between \$100,000 and \$500,000 []
More than \$500,000 []

III. BONDING

Is Member required to have a fidelity bond?

Yes [] No []

Name of insurance company: _____

IV. PENDING INVESTIGATION(S) AND/OR LITIGATION(S)

Is the Member the subject of any investigation(s), hearing(s), injunction(s), operational restriction(s) or other actions by a regulatory body? Yes _____ No _____

Is the Member currently involved in any litigation of a criminal or civil nature? Yes _____ No _____

DATE: _____ SIGNATURE: _____

II. GUIDELINES FOR COLLECTING CLEARING FUND DEPOSITS FOR SETTLING MEMBERS NOT ON SURVEILLANCE STATUS

- A. Clearing Fund deposits for Settling Members are computed on a daily basis; except as specified below, however, Settling Members not on surveillance status shall be required to make any additional Clearing Fund deposits on a monthly basis.
- B. To the extent a Settling Member's Clearing Fund requirement increases by ten (10) percent (or \$10,000 for a Member with a Clearing Fund requirement of less than \$100,000), the Corporation may require the Settling Member to make an additional Clearing Fund deposit sooner than on a monthly basis.
- C. In addition to paragraph B above, as part of its monitoring of Clearing Fund deposit requirements, on a daily basis the Corporation will determine whether changes in Settling Member's required deposits break certain percentage thresholds for the portion of the Clearing Fund deposit relating to CNS activity. These thresholds are:
 - 1. the current Clearing Fund requirement (based on the previous twenty (20) business days' activity) for CNS activity is more than twenty-five (25) percent higher than the previous month-end requirement;
 - 2. the average of the last five (5) calculations described in paragraph (C)(1) immediately above is more than fifteen (15) percent higher than the previous month-end requirement.
- D. If the CNS Clearing Fund requirement exceeds either of the thresholds in paragraph C, and if, as a result, a Settling Member's deposit is insufficient to cover this

(ADDENDUM B - 21)

increase (and the deficiency is at least ten (10) percent of the deposit or \$10,000), the Corporation will require payment of the deficiency sooner than on a monthly basis.

- E. The Corporation may grant exemptions to the requirement that deficiencies in the Clearing Fund deposits resulting from the application of paragraphs C and D above be paid prior to month-end if the Corporation determines that the Settling Member does not pose additional risk to the Corporation that would require such an additional deposit prior to the month-end review.

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- F. The Corporation may require a Fund/Serv Broker-Dealer to make an additional Clearing Fund deposit sooner than on a monthly basis if such Member's Clearing Fund requirement increase at least \$5,000.

III. GUIDELINES FOR DETERMINING WHEN THE CORPORATION MAY PLACE A SETTLING MEMBER OR SECURITY ON SURVEILLANCE STATUS

A. All Settling Members

1. "Advisory" Surveillance Status

a. Any condition which could materially impact the operational and financial viability of a Settling Member which increases or may potentially increase exposure to the Corporation and which does not meet the parameters of Class "A" or "B" surveillance status;

b. a 50% increase in average daily debits and credits calculated weekly over the average daily debits and credits for the previous calendar month;

c. when a Federal banking agency serves a Settling Member with a permanent cease and desist order pursuant to Section 8(b) of the Federal Deposit Insurance Act regarding any violation of a law, rule or regulation or any unsafe or unsound practice which could bring into question the continued financial or operational capability of the Settling Member to continue to fulfill its obligations to the Corporation;

d. when the sum of the average daily Envelope Settlement System² debits plus the average daily Qualified Securities Depository debits of a Sponsored Member not eligible to use the Alternative Clearing Fund Formula set forth in section XV, subsection A.II.(a) exceeds such Sponsored Member's excess net capital.

B. Broker/Dealer Settling Members

1. Class "A" Surveillance Status

a.(i) Firms computing net capital under basic method having a capital ratio exceeding 9.5 to 1 (950%), but not greater than 10.5 to 1 (1050%);

² As used in this subsection III.(A)(1)(d), the term "Envelope Settlement System" shall mean such non-CNS activity, other than DTC Sponsored Account activity, as the Corporation may determine from time to time.

- (ii) firms computing net capital under alternative method having capital percentage less than or equal to 5.25% but not less than 4.0%;
- b. net losses in a one-month period of 15% or more of a Settling Member's excess net capital, two-month period of 25% or more, three-month period of 30% or more; or, a reduction in excess net capital of 25% or more in one month attributable to, among other things net losses, increased haircuts, charges to capital or repayment of subordinated loans;
- c. temporary inability by a Settling Member to meet settlement obligations in a timely manner or a potential cash flow problem indicated by late daily settlement, payment in uncertified funds, overnight suspense items or a continuous negative unrestricted cash position per monthly financial data received;
- d. Settling Member has declared itself to be self-liquidating, merging, being acquired or otherwise retiring and has a history of previous surveillance or financial problems;
- e. potential operational problems of a Settling Member indicated by a significant increase in the number of advisories accepted or an unusual number of DK's or reclaims;
- f. notification by Designated Examining Authority of a pending administrative action or investigation of a Settling Member which could bring into question the continued financial or operational capability of the Settling Member to continue to fulfill his obligations to the Corporation;
- g. Settling Member has two or more unexcused late or materially adjusted monthly financial reports in an 18-month period;
- h. during any two consecutive months, the Settling Member's net capital is equal to or less than 150% of either the SEC's minimum requirement or, if higher, its Designated Examining Authority's basic minimum requirement for a broker/dealer who conducts a general securities business or the Settling Member's equity is equal to or less than 35% of its total capitalization;
- i. any CNS position(s) (Long or Short) of a Settling Member disproportionate to his usual CNS activity;
- j. Settling Member is on any closer-than-normal or special surveillance list by another self-regulatory organization, or any other material data concerning a

Settling Member which could impact the Settling Member's financial or operational viability as a participant;

k. material increase or change in volume, fails, aged fails, inventory, customer exposure, nature of business (i.e., market making activity, underwriting, options, etc.) of a Settling Member without corresponding increases in profitability, or changes in net capital or excess net capital monitored over a period of three or more months;

l. reorganization of firm due to merger, acquisition, and changes in management which may, but do not necessarily, result in negative capital impact;

m. firm clearing for other firms which is instructed by its Designated Examining Authority to reduce or eliminate some or all of such activity;

n. firm with large CNS position in an issue halted, suspended or under investigation by a self-regulatory organization or the Securities and Exchange Commission;

o. any other condition which could materially impact the operational or financial viability of a Settling Member which increases or may potentially increase exposure to the Corporation.

2. Class "B" Surveillance Status

a.(i) Firms computing net capital under basic method having a capital ratio exceeding 10.5 to 1 (1050%);

(ii) firms computing net capital under alternative method having a capital percentage of less than 4%;

b. net losses in a one-month period of 30% or more, two-month period of 50% or more of a Settling Member's excess net capital or a reduction in excess net capital of 40% or more in one month attributable to among other things: net losses, increased haircuts, changes to capital or repayment of subordinated loans;

c. Settling Member is a Section 5(a) referral to SIPC or Settling Member is filing pursuant to Rule 17a-11;

d. during any two consecutive months, the Settling Member's net capital is equal to or less than 120% of either the SEC's minimum net capital requirement or, if higher, its Designated Examining Authority's basic minimum requirement for a broker/dealer who conducts a general securities business or the Settling Member's equity is equal to or less than 30% of its total capitalization;

e. any CNS position(s) (Long or Short) of a Settling Member which is continually and materially disproportionate to his usual CNS activity;

f. any condition of a Settling Member in Class "A" which significantly deteriorates so as to impact the Settling Member's excess net capital.

C. Bank Settling Members

I. Class "A" Surveillance Status

a. A decline in consolidated net income (after securities gains and losses) in the course of a fiscal year or two consecutive fiscal years amounting to more than 50% of such consolidated net income for the preceding fiscal year, unless the Settling Member's capital is 5% or more of its total assets at the end of the relevant fiscal year(s) in which such consolidated net income has declined, or he or his parent bank holding company maintains a Moody's or Standard & Poor's bond rating of at least A, or commercial paper rating of at least P2 or A2;

b. a consolidated net loss (after securities gains and losses) in any fiscal year;

c. temporary inability by a Settling Member to meet settlement obligations in a timely manner indicated by late daily settlement or overnight suspense items;

d. potential operational problems of a Settling Member indicated by a significant increase in the number of advisories accepted or an unusual number of DK's or reclaims;

e. when a Federal banking agency serves a Settling Member with a temporary cease and desist order pursuant to section 8(c) of the Federal Deposit Insurance Act regarding any violation of a law, rule or regulation or any unsafe or unsound practice which could bring into question the continued financial or operational capability of the Settling Member to continue to fulfill its obligations to the Corporation;

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f. any CNS position(s) (Long or Short) of a Settling Member disproportionate to his usual CNS activity;

g. a material increase or change in volume or in the nature of business which involves additional use of the Corporation's services without corresponding increases in profitability, or corresponding additions to capital over a period of three or more months;

h. firm clearing for other firms which is instructed by a Federal banking agency to reduce or eliminate some or all of such activity;

i. firm with large CNS position in an issue halted, suspended or under investigation by a self-regulatory organization or the Securities and Exchange Commission;

j. when a Settling Member's financial condition is such that the Settling Member must obtain the consent of a bank regulatory authority to pay dividends in excess of an amount equal to 50% of the average amount of dividends paid in the past two years;

k. any other condition which could materially impact the operational or financial viability of a Settling Member which increases or may potentially increase exposure to the Corporation.

2. Class "B" Surveillance Status

a. When a Settling Member's financial condition is such that the Settling Member is prohibited from paying dividends by or pursuant to the banking law under which it is chartered;

b. net losses in any fiscal quarter or fiscal year exceeding 10% of a Settling Member's capital;

c. when a Settling Member seeks or receives financial assistance from the Federal Deposit Insurance Corporation pursuant to Section 13(c) or (e) of the Federal Deposit Insurance Act;

d. any CNS position(s) (Long or Short) of a Settling Member which is continually and materially disproportionate to his usual CNS activity;

e. when a Federal banking agency serves a director or officer of a Settling Member with a written notice of intent to remove that person from office pursuant to Section 8(e)1 or 8(e)2 of the Federal Deposit Insurance Act;

f. the assessment of any penalty upon a Settling Member pursuant to Section 8(i) of the Federal Deposit Insurance Act for any violation of the terms of a cease and desist order issued by a Federal banking agency or a consent agreement entered into with a Federal banking agency under circumstances which could bring into question the continued financial or operational capability of the Settling Member to continue to fulfill its obligations to the Corporation;

g. when the Federal Deposit Insurance Corporation serves a Settling Member with written notice of intent to terminate the Settling Member's federal deposit insurance pursuant to section 8(a) of the Federal Deposit Insurance Act;

h. when a Settling Member receives extended credit from the Federal Reserve discount window other than seasonal credit;

i. any condition of a Settling Member in Class "A" which significantly deteriorates so as to impact the Settling Member's financial condition.

D. Securities

1. Class I Security Surveillance Status

a. Volume and/or price movement results in trading halt, temporary suspension, stock watch alert or warning by the SEC or another self-regulatory organization;

b. special or increased initial margin requirement imposed by a self-regulatory organization or security is a recent addition to the approved list of margin securities;

c. security has been delisted by a national securities exchange, or NASDAQ, or has been delisted by the Federal Reserve Board for margin; or delisting proceedings have been initiated by any of the above entities;

d. issuer is the subject of a petition under any provision of the Bankruptcy Code;

e. security is subject to offer of merger, acquisition, tender offer, call or risk arbitrage situation or security is traded, in the Corporation's opinion, in an unusually thin market;

- f. substantial increase in an active Short Position of an issue, where there has been a large adverse price movement, particularly with respect to usually inactive issues;
- g. issue or issuer is the subject of a market surveillance, stock watch or regulatory report by a self-regulatory organization or the subject of a formal order of investigation by the SEC;
- h. securities, the liquidation of which would create a disorderly market in that security;
- i. a security position in the CNS system of a Settling Member, which is of such a size as might threaten to create a disorderly market in the event of a closeout.

2. Class II Security Surveillance Status

- a. Any sustained activity of a stock in Class I which may have an inordinate financial impact on the Corporation and/or its Settling Members.

IV. GUIDELINES FOR COMPUTING CLEARING FUND DEPOSITS FOR SETTLING MEMBERS ON SURVEILLANCE STATUS OTHER THAN MUNICIPAL SECURITIES BROKERS' BROKERS THAT HAVE A SPONSORED ACCOUNT AND WHO ELECT THE ALTERNATIVE CLEARING FUND FORMULA.

- A. Clearing Fund deposits for Settling Members on surveillance status shall be computed on a daily basis;
- B. Clearing Fund deposits for Settling Members on "Advisory" Surveillance Status shall be comprised of the normal CNS clearing fund requirement plus, 2-1/2% or in the discretion of the Corporation up to 5% of the Settling Member's average daily settlement debits, excluding CNS and Mutual Fund Services debits, plus 2-1/2% of the average daily settlement credits, excluding CNS and Mutual Fund Services credits;
- C. Clearing Fund deposits for Settling Members on Class "A" Surveillance Status shall be comprised of the normal CNS clearing fund requirement plus, (i) up to 5% of the Settling Member's CNS Long fail positions, plus (ii) up to 5% of the Settling Member's CNS Short fail positions, plus (iii) 2-1/2% or in the discretion of the Corporation up to 5% of the Settling Member's average daily settlement debits,

excluding CNS and Mutual Fund Services debits, plus 2-1/2% of the Settling Member's average daily settlement credits, excluding CNS and Mutual Fund Services credits;

- D. Clearing Fund deposits for Settling Members on Class "B" Surveillance Status shall be comprised of the normal CNS clearing fund requirement, plus (i) up to 10% of the Settling Member's CNS Long fail positions, plus (ii) up to 10% of its CNS Short fail positions, plus (iii) an additional percentage, as determined by the Corporation, of the Settling Member's average daily settlement debits and/or credits, excluding CNS and Mutual Fund Services debits and/or credits;
- E. Additional Clearing Fund deposits for Settling Members on surveillance shall not be required where the amount of the deficiency is less than \$1,000. Where the amount of the deficiency is in excess of \$1,000 but less than \$5,000 the Corporation shall require payment in multiples of \$1,000. Where the amount of the deficiency is in excess of \$5,000 the Corporation shall require payment in multiples of \$5,000. Notwithstanding the foregoing, the Corporation generally will not require additional deposits unless the amount of the deficiency is equal to or greater than 10% of the Settling Member's Clearing Fund deposit;
- F. Excess Clearing Fund deposits shall be refunded on a quarterly basis, provided, however, that the Corporation may, but shall not be required to, make refunds at the request of the Settling Member, prior to the end of the quarter.

V. GUIDELINES FOR COMPUTING CLEARING FUND DEPOSITS FOR MUNICIPAL SECURITIES BROKERS' BROKERS THAT HAVE A SPONSORED ACCOUNT AND WHO ELECT THE ALTERNATIVE CLEARING FUND FORMULA AND ARE ON SURVEILLANCE

- A. Clearing Fund Deposits for Sponsored Account Municipal Securities Brokers' Brokers Members on surveillance status who elect the Alternative Clearing Fund Formula shall be computed on a daily basis.
- B. The Corporation, in its discretion, may require a Sponsored Account Municipal Securities Brokers' Broker Member on surveillance status who elects the Alternative Clearing Fund Formula to meet Clearing Fund requirements set forth in Section IV above or such lesser amounts as the Corporation may in its discretion require.
- C. Additional Clearing Fund deposits for Sponsored Account Municipal Securities Brokers' Brokers Members on surveillance status shall not be required where the amount of the

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deficiency is less than \$1,000. Where the amount of the deficiency is in excess of \$1,000 but less than \$5,000 the Corporation shall require payment in multiples of \$1,000. Where the amount of the deficiency is in excess of \$5,000 the Corporation shall require payment in multiples of \$5,000. Notwithstanding the foregoing, the Corporation generally will not require additional deposits unless the amount of the deficiency is equal to or greater than 10% of the Member's Clearing Fund deposit.

- D. Excess Clearing Fund deposits shall be refunded on a quarterly basis, provided, however, that the Corporation may but shall not be required to make refunds at the request of the Member, prior to the end of the quarter.



National Securities Clearing Corporation

Introduction

National Securities Clearing Corporation (NSCC) is the nation's leading provider of centralized clearance, settlement and information services for equity, corporate and municipal bond, Unit Investment Trust (UIT) and mutual fund transactions. NSCC now clears and settles 98% of all equity and bond transactions in the United States and plays a critical role in the safety and soundness of the markets.

International Securities Clearing Corporation (ISCC), a wholly owned subsidiary of NSCC formed in 1985, provides clearance and settlement services to U.S. brokers trading in overseas markets. *Government Securities Clearing Corporation (GSCC)*, an NSCC affiliate established a year later, brings the efficiencies of automated clearance and settlement to brokers, dealers and banks trading in the U.S. Government securities marketplace. *MBS Clearing Corporation (MBSCC)*, which was established in 1979 and became jointly owned by its participants and NSCC in 1994, facilitates the post-trade activities of the mortgage-backed securities market.

NSCC is owned equally by the New York Stock Exchange (NYSE), the American Stock Exchange (Amex) and the National Association of Securities Dealers Inc. (NASD), and is registered as a clearing agency with the Securities & Exchange Commission (SEC). The Company's primary mission is to develop high-quality, innovative, dependable systems and services that meet the financial industry's requirement for cost-effective, high-volume trade processing that helps minimize risk.

NSCC works closely with the Securities Industry Automation Corporation (SIAC), its facilities manager; and The Depository Trust Company (DTC), a central depository that holds participants' securities and makes receipts and deliveries in book-entry form. The Company anticipates the expanding and ever-changing needs of the industry through its active, positive communications with the securities exchanges; the SEC and other government regulatory agencies; and the financial services firms that are NSCC's customers.

NSCC History & Structure

NSCC began operating in 1976, with the consolidation of the clearing operations of the NYSE, Amex and NASD. The Company was created to address the existing and evolving post-trade processing needs of broker/dealers and banks, and has since expanded its services to include the mutual fund community.

NSCC operates as a user-driven corporation. The firm's senior management is guided by its Board of Directors, which works closely with management in policy development, operational planning and financial management. The Board is made up of 19 members: 15 Participant Directors elected from participating brokers, dealers, banks and mutual funds; NSCC's President and Chief Executive Officer; and three Shareholder Directors.

NSCC Participants

More than 1,900 brokers, dealers, banks, mutual funds and other financial institutions currently use NSCC's services as direct participants, as regional participants through the Regional Interface Operation (RIO), or as indirect participants through Correspondent relationships.

NSCC Communications

NSCC provides its services through a variety of data transmission capabilities including CPU-to-CPU links and PC access for selected applications, via electronic interfaces with other clearing corporations and through branch offices. NSCC supports a reliable and sophisticated communications network that includes two data processing sites for redundancy and a tested disaster-recovery program.

NSCC Risk Management

Guaranteeing the financial settlement of transactions is a central function of NSCC, and one that eliminates uncertainty in the marketplace. NSCC nets participants' transactions into one position per issue, then interposes itself in the middle of each net transaction. Through its Continuous Net Settlement (CNS) System, NSCC guarantees settlement for eligible transactions as of midnight of the day the trade is reported to members as compared. NSCC limits the risk arising from this process by maintaining high membership standards, closely monitoring participants' positions and market conditions, marking securities to market, and carefully managing its Clearing Fund.

The Clearing Fund was established to secure participants' obligations to NSCC and other liabilities and losses should they occur. Participants are required to contribute to the Clearing Fund according to a formula established by the Board. Clearing Fund deposits can be in cash, U.S. Treasury securities, or in Letters of Credit issued by authorized banks (in cases where letters of credit are used, certain cash minimums must also be maintained).

NSCC Products & Services

NSCC products and services center on post-trade processing of equity, corporate and municipal bond, UIT, and mutual fund transactions. The post-trade processing component of NSCC's business involves two steps: Comparison and Recording, or matching the buy and sell sides of transactions and recording compared trade obligations from securities marketplaces; and Settlement, or the transfer of money and securities to settle trade obligations.

Steps In Post-Trade Processing**Comparison**

In the comparison process, NSCC matches detailed transaction information submitted by the buyer and the seller, in order to establish binding contracts for settlement. Details are submitted on trade date, and results of the matching process are reported to participants one day after the transaction takes place; these transactions are said to have "cleared" and subsequently settle on the third business day after execution. Transactions that initially do not match are reported to participants for correction. NSCC and the securities marketplaces have instituted standardized procedures for participants to use to correct trade differences.

Equities

NSCC's equity trade comparison service handles transactions executed on the NYSE, Amex and OTC marketplaces, and includes domestic (U.S.) as well as foreign equity securities (via NSCC's Foreign Securities Comparison & Netting System). In addition, trades executed at regional exchanges can be routed to NSCC for settlement via the Regional Interface Operation (RIO).

Increasingly, transactions are submitted to NSCC via a variety of automated marketplace trading systems, and are reported to NSCC as "locked-in" trades that already have been compared. Transactions that are not locked-in are compared in either NSCC's Listed Comparison System (for trades involving exchange-listed securities) or its OTC Comparison System (for transactions in the over-the-counter market).

The Foreign Securities Comparison and Netting System automates the comparison process for foreign securities traded in ordinary shares. The system allows foreign securities traded between two NSCC members to be compared and netted participant-to-participant, using a common settlement price. The securities are processed in NSCC's OTC Comparison System, with trade details submitted in the same manner as those for U.S. OTC transactions.

Fixed Income

NSCC's Fixed Income Transaction System (FITS) provides efficient and standardized processing of municipal and corporate bonds and UITs, by allowing the submission of trades on trade date. This enables timely trade comparisons and early resolution of discrepancies by participants, and also reduces risk. As with equities, fixed income trades increasingly are received by NSCC as "locked-in" by automated trading systems.

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NSCC's three settlement systems. The vast majority of transactions are settled through the CNS System, which allows the netting of transactions and the automatic book-entry movement of depository-eligible securities in a centralized, controlled and fully automated environment. The Balance Order System is used largely for settlement of non-depository-eligible issues. Trade-For-Trade Settlement allows individual trades to be settled separately, bypassing the netting process.

Continuous Net Settlement

Securities that are eligible for depository processing through DTC enter the CNS System. This automated book-entry settlement system relies on an interface between NSCC and DTC for the movement of book-entry shares among participants, in order to settle accounts.

All current transactions in CNS are netted daily by participant into one position per issue, and then are further netted with any open obligations. NSCC is the contra side to each settling CNS transaction, and guarantees settlement to both sides of every CNS compared trade. Next, NSCC instructs DTC to move securities from the accounts of the net sellers to the NSCC account, and the securities are then allocated to the accounts of the net purchasers. Finally, NSCC nets the dollar value of CNS securities movements to generate a net CNS money settlement, which is consolidated with other NSCC settlements to produce a net debit or credit position for each participant every business day.

Additional CNS Services

NSCC offers several services through the CNS System to help participants in their processing.

- *The Stock Borrow Program* allows participants to lend excess securities in their DTC accounts to NSCC to cover temporary shortfalls in the CNS System. NSCC credits the member's money settlement account with the full current market value of the borrowed securities, and members can invest these funds to earn overnight interest.
- *The Fully-Paid-For Account and Expanded Fully-Paid-For Account* help participants reduce "iffy" borrows and unnecessary carrying costs through the controlled use of customer securities (excluding municipal bonds) when the firm expects a CNS allocation from NSCC in the same security.
- *Reorganization Sub-Accounts* allow participants to benefit from the netting process by enabling them to take part in mandatory reorganizations and voluntary tender and exchange offers through CNS.
- *The ID/CNS Interface for Prime Broker Business* streamlines the processing of trades executed by one party (the Executing Party) on behalf of an institutional customer who instructs that the trade be forwarded to another party (the Prime Broker) for clearance and settlement. The interface allows both parties to benefit from netting and reduced securities movements provided by CNS.
- *The Correspondent Clearing Service* simplifies the processing of transactions executed by one participant (the Special Representative) on behalf of another participant (the Correspondent) by transferring the settlement obligation to the Correspondent, eliminating the need for redeliveries and decreasing the potential for errors in the accounting and settlement process.
- *NSCC's Canadian Depository for Securities (CDS) Link* provides a book-entry clearance and settlement system for DTC-eligible securities traded between CDS and NSCC members.
- *The Reconfirmation and Repricing Service (RECAPS)* is an automated fail clearance system that reconfirms and reprices participants' aged equity, municipal bond and zero coupon issue fails previously compared by NSCC or other means.

Physical Settlement: The Balance Order System

Securities that are not eligible for depository processing through DTC can be settled through NSCC's Balance Order System, a physical securities processing system. In this system, NSCC nets each participant's receive and deliver obligations into a single position per issue every day. NSCC then allots the securities, assigning a deliverer and receiver based on net positions. The Balance Order System centralizes and streamlines processing of physical securities and funds and reduces securities deliveries.

Additional Physical Settlement Services

NSCC provides a number of services to assist participants in processing their physical deliveries in a safe and cost-effective manner.

- *The Envelope Settlement Service (ESS) and Intercity Envelope Settlement Service (IESS)* standardize and control the movement of certificates, and ensure that participants receive either money settlement credit or their certificates.
- *Direct Clearing* allows regional participants without a New York office to settle physical securities using NSCC's envelope settlement services. It also facilitates over-the-window deliveries.
- *The Funds-Only Settlement Service (FOSS)* centralizes the routing of envelopes containing money-only charges (primarily debits and credits resulting from mark-to-market adjustments) among full-service NSCC participants in New York City, N.Y. and Jersey City, N.J.
- *The Dividend Settlement Service (DSS)* is a claims-processing system that facilitates the efficient collection of cash dividends and registered bond interest owed between NSCC members.
- Through the *National Transfer Service (NTS)*, NSCC efficiently and economically moves various items to transfer agents within a network of cities throughout the U.S. and Canada. NTS handles securities that result from trading activities, as well as book-closing items, legal transfers and accommodation transfers.

Trade-For-Trade Settlement

Trade-For-Trade Settlement allows participants to settle individual trades separately at the contract price. Trade-for-trade settlement can be utilized if both participants use a special trade indicator at the time the trade is submitted. This prevents the trade from entering the netting system and creating a receive or deliver order. Trade-for-trade transactions settle separately from CNS and balance order transactions.

How Money Settles

Money Settlement is the final stage of the comparison and settlement process. In money settlement, NSCC centralizes and nets credit and debit obligations for each participant, so that settlement can be achieved in one transaction. Each participant makes payment to or collects payment from NSCC each day to bring their NSCC account to zero. NSCC also cross-endorses settlement with DTC, so that joint NSCC/DTC members can gain the maximum benefit of netting between the two organizations.

Managing Collateral

NSCC's Collateral Management Service (CMS) provides members with information on their own clearing fund and margin deposits and requirements at NSCC and at other participating clearing entities. Members using CMS can determine if they have an excess or deficit at any of the participating clearing entities and through a PC access detailed data on their collateral.

Other NSCC Services

Responding to Change

Today, NSCC offers a number of services that meet changing industry requirements yet remain consistent with the Company's charter to help minimize risk, standardize and eliminate redundant functions, and reduce firm operating costs.

Mutual Fund Services

In the mid-1980s, mutual fund transaction processing was a paper-intensive, costly manual process. Facing questions about its ability to handle continued growth, the industry sought NSCC's help in developing automated solutions. NSCC's Mutual Fund Services automate and standardize mutual fund-related processing, facilitating growth in the industry by providing the operational efficiencies that are NSCC's hallmark.

- NSCC's *Fund/SERV* is a central processing system that enables mutual funds and broker/dealers to enter, confirm, settle and register mutual fund purchase and redemption orders in an efficient and automated environment. The system also can accommodate the special, volume-related needs of underwritings and tender offers.

- *Networking* is an automated, centralized recordkeeping system through which all customer account-level information other than order processing can be exchanged between broker/dealers and mutual funds.
- *The Commission Settlement Service* is an automated system that facilitates the exchange of mutual fund commission-related information between brokers and funds, and allows mutual fund commission payments to enter NSCC's settlement system.

Account Transfers

NSCC designed the Automated Customer Account Transfer Service (ACATS) in 1985 to address the problems of delays caused by the manual transfer of brokerage industry customer accounts. ACATS automates this process, providing a vehicle for the efficient and timely transfer between brokers of customers' cash or margin accounts, as well as Individual Retirement Accounts (IRAs) or Qualified Corporate Plans (Keoghs).

Options positions in an account are passed through ACATS to The Options Clearing Corporation (OCC) for transfer. The ACATS - Fund/SERV Interface allows participants to reregister mutual fund assets transferred through ACATS.

New York Window

The New York Window is a platform of services that supports the clearance of physical securities for brokerage and banking institutions. Services include receipt and delivery of securities over-the-window or through branch receives and NSCC's envelope services, physical transfers and reorganizations, underwritings, processing of DTC withdrawals and deposits, end-of-day settlement, and messenger services. To complement these services, custody services also are offered.

Commission Billing

Commission Billing provides an automated facility for the debiting and crediting of commissions owed among NSCC full-settling members and NYSE and Amex specialists and floor brokers. NSCC members can submit commission bill debit lists to NSCC for payment from their NSCC accounts. Specialists and floor brokers benefit from receiving or making one monthly payment from or to NSCC.

PC Platform

PC Platform is a cost-effective and user-friendly data entry and communications package that allows participants to transmit data from a personal computer to NSCC's state-of-the-art processing system, and receive activity reports on their PC. With PC Platform, users can input information directly into six NSCC services — ACATS, CNS, Correspondent Clearing, FITS, RECAPS, and Commission Billing. The single-user system can be installed on most DOS-based personal computers with an 80386SX or higher class processor.

NSCC Fees

NSCC provides the financial services industry with high-quality services at reasonable cost. Service fees, which are set by the Board of Directors and filed with the SEC, are charged on a cost-related basis. The Company is committed to carefully managing operating costs, and is constantly exploring new ways to achieve economies of scale that will allow cost savings and fee reductions for members. NSCC's current fee structure for all products and services is available upon request.

NSCC Marketing

NSCC Marketing Representatives are available to provide further information about the Company's systems and services, structure, fees, and operations. Please contact:

National Securities Clearing Corporation
55 Water Street, 22nd Floor
New York, N.Y. 10041
(212) 412-8432 (Tel.)
(212) 412-8495 (Fax)



Stock Borrow Program

The **Stock Borrow Program** allows participants to lend NSCC available stocks and corporate bonds from their account at the Depository Trust Company (DTC), to cover temporary shortfalls in NSCC's Continuous Net Settlement (CNS) System. NSCC credits members' money settlement accounts with the full market value of securities borrowed, and members can earn overnight interest on that value by investing the funds. In addition, members can enhance securities inventory management in a safe, controlled environment through the program.

Who can use the service

All NSCC members, including brokers, dealers, banks, and other financial institutions, can participate in the Stock Borrow Program. Stocks and corporate bonds are eligible for the program.

Benefits

- The Stock Borrow Program enables participants to earn interest on the full current market value of their excess DTC positions borrowed by NSCC, while lending securities in the safety of a controlled environment.
- In the Stock Borrow Program, participants' NSCC money settlement accounts are credited on the day of the loan with the full market value of any securities borrowed by NSCC. This allows members to invest the funds to earn interest overnight on the value received from the loans.
 - Securities on loan to NSCC are recorded as long positions in a special CNS account set up specifically for the participant's Stock Borrow activity. This enables the member to benefit from lending securities within the safe, controlled CNS processing environment.

How the service works

By early evening on each business day, participants forward to NSCC a list of securities that are available for borrowing. The list can be transmitted via CPU-to-CPU link or PC Platform. Early in the morning on the following business day, NSCC determines the high-priority securities obligations that remain open after the first segment of CNS clearance processing. NSCC then attempts to satisfy these obligations by borrowing from participants in the Stock Borrow Program.

Selecting Lenders

If two or more participants are willing to lend the same security, NSCC selects one based on an algorithm which takes into account a random number and the participant's average loans and clearing fees. This procedure permits borrowing to be spread among many potential lenders of a security. NSCC uses the full quantity that the participant makes available in each issue before proceeding to the next participant in the sequence.

Crediting Participants' Accounts

After NSCC borrows securities in the evening, the transactions are recorded as long positions in the participant's Stock Borrow (C) sub-account, a special account in the CNS System. The total current market value of the borrowed securities is credited in the participant's CNS account. These funds are available to the participant overnight. This process is reversed when NSCC returns the borrowed securities. No rebates are charged and the entire transaction occurs in the controlled CNS processing environment.

Reporting On Stock Borrow Activity

NSCC distributes reports to participants each morning, reflecting Stock Borrow activity. In reviewing the report, participants sometimes discover that the securities lent to NSCC place the firm in violation of Securities & Exchange Commission (SEC) regulations concerning the segregation of fully-paid-for customer

es, the deficit can be covered by transferring the [redacted] the Stock Borrow
account into the [redacted] position in the Fully-Paid-For (E) account. This results in the [redacted] member being debited the
current market value of the securities position. The Securities & Exchange Commission treats this "E" posi-
tion as a good control location for customer securities under Commission rule 15c3-3.

For more information

Please contact NSCC's Participant Services at (212) 412-8432.

*The Stock Borrow Program is a service offering of National Securities Clearing Corporation, the nation's
leading provider of centralized clearance, settlement and information services to more than 1,900 brokers,
dealers, banks, and mutual funds.*

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Attachment G.

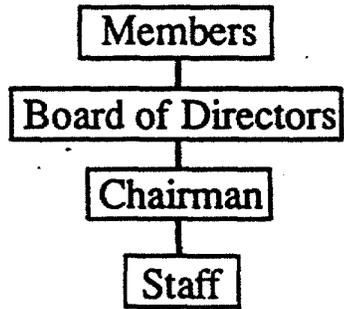
New York Stock Exchange-

(1) Corporate Structure

(2) U.S. Equity markets and the NYSE

(3) Constitution and Rules

CORPORATE STRUCTURE



S

MEMBERS

- 1,366 equity members
- Physical access members
- Electronic access members
- Lessee members



BOARD OF DIRECTORS

Powers

- Makes rules for all aspects of members' business
- Has supervision over members and member firms in their business conduct, their offices and business connections
- Approves applications for listing securities at NYSE
- Discipline of members

NYSE

COMPOSITION

24 Directors plus chairman, executive vice chairman,
and president

Public Directors (12)

- Listed company representatives
- Institutional investor representatives

NYSE

85

COMPOSITION

Industry Directors (12)

- Representatives of NYC member firms that do a substantial business with securities customers (5)
- Representatives of member firms located outside NYC that do business with the public (2)
- Registered specialists (3)
- Representative of NYC specialty firm (1)
- Floor member (deals for own account) (1)

The NYSE logo, consisting of the letters "NYSE" in a bold, serif font, positioned to the right of two horizontal lines.

86

CHAIRMAN

- Chief Executive Officer
- Responsible for management and administration of NYSE affairs
- Official NYSE representative in all public matters

The NYSE logo, consisting of the letters "NYSE" in a bold, serif font, with horizontal lines through the letters.

81

BOARD ADVISORY COMMITTEES

- Exchange Traders Advisory Committee
- Institutional Traders Advisory Committee
- Advisory Committee of Upstairs Traders
- Regional Firms Advisory Committee
- Specialty Firms Advisory Committee
- Individual Investors Advisory Committee
- Pension Managers Advisory Committee

NYSE

AS

BOARD ADVISORY COMMITTEES

- Advisory Committee on International Capital Markets
- European Advisory Committee
- Japan Advisory Committee
- Legal Advisory Committee
- Regulatory Advisory Committee
- Listed Company Advisory Committee

NYSE

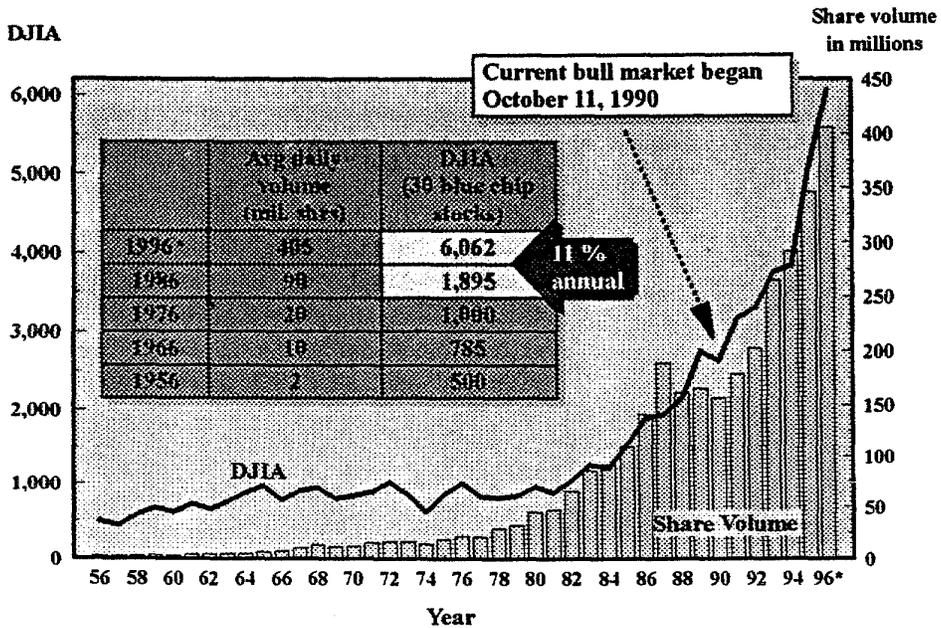
U.S. Equity Markets and the New York Stock Exchange

George Sofianos
October 23, 1996

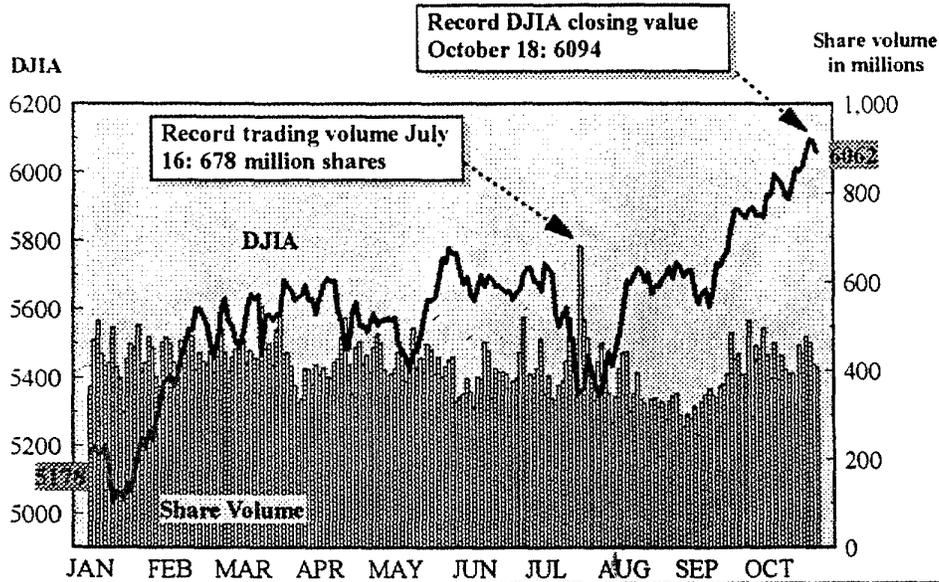
gsofianos@nyse.com



DJIA and NYSE share volume, 1956 - 1996



1996 daily DJIA closing values



Through October 22, 1996

In 1995 equity prices were up 35 percent
In 1996 equity prices are up 16 percent

Auction and dealer markets



- **Dealer markets**
 - public orders are filled by dealers

- **Auction markets**
 - public orders trade with public orders with no dealer intervention

Examples of dealer markets

- ▶ Foreign exchange
- ▶ U.S. Treasuries
- ▶ Nasdaq
- ▶ London Stock Exchange

Examples of auction markets

- ▶ Bombay Stock Exchange
- ▶ Paris Stock Exchange
- ▶ Toronto Stock Exchange

The NYSE is mostly an auction market

- ▶ some dealer participation
- ▶ trading floor

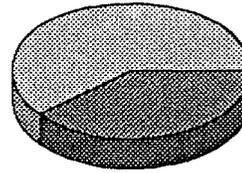
Listed and unlisted stocks



- **Listed stocks**
 - NYSE, AMEX
 - regional exchanges: BSE, CHX, CSE, PHLX, PSE
- **Unlisted stocks trading in the over-the-counter market**
 - Nasdaq
 - Bulletin Board
 - Pink Sheets

1995 Dollar Volume

Listed 61%



Nasdaq 39%

Listed includes NYSE and AMEX consolidated; Nasdaq does not include Bulletin Board and Pink Sheets

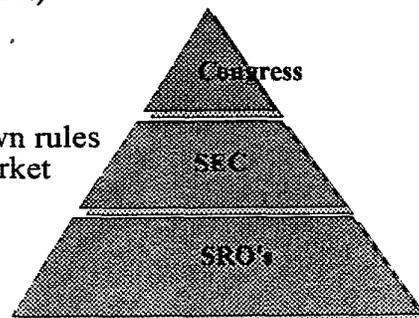
Regulation of U.S. equity markets



Main objectives

- ▶ investor protection and market efficiency

- **Legal framework provided through Congressional Acts**
 - Securities Act of 1933 and Securities Exchange Act of 1934
 - Securities Acts Amendments of 1975
- **Securities and Exchange Commission (SEC)**
 - government agency
 - monitors and enforces regulation
- **Self Regulating Organizations (SRO's)**
 - NYSE and other exchanges have their own rules
 - NASD regulates the over-the-counter market
 - SRO rules subject to SEC approval



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Corporate structure of the NYSE



- A not-for-profit corporation
- Governed by Board of Directors
 - 12 securities industry directors
 - 12 public directors *Issuers, Institutional/Retail Investors*
 - 2 full-time officers
- Owned by its members
- 1,366 membership seats
 - 482 member firms*
 - number of seats unchanged since 1953

NYSE had problems of image with only board of governors belonging to the securities industry.

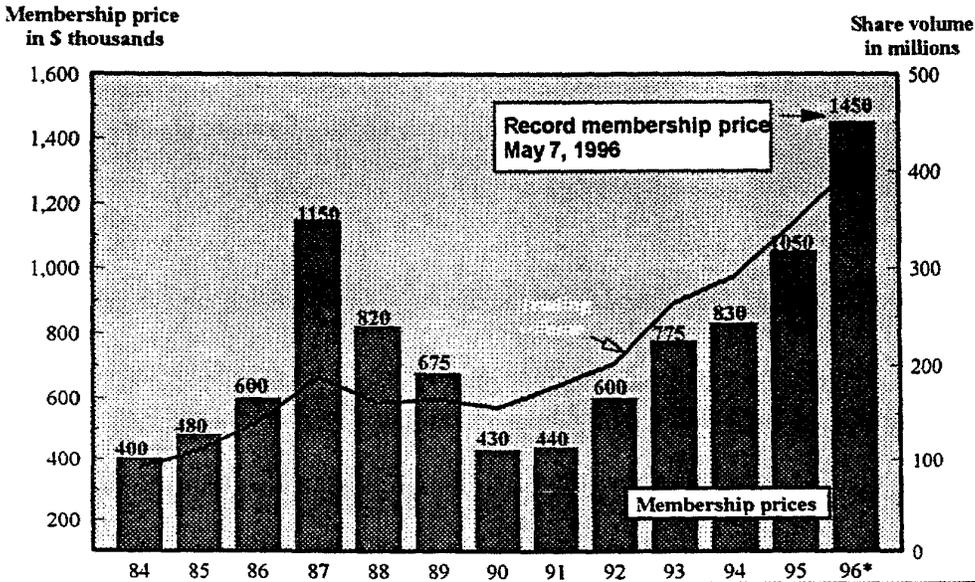
lots of many seats for a firm

*no. of floor brokers or no. of seats
 come out of mergers Investments as seats can
 IBM Book + list sold for 10m. \$ to sold.*

How do you become an NYSE member?

* Through September 30, 1996.

NYSE membership prices



1.6 million

Record membership price May 7, 1996

Most recent membership price \$1.16 million on September 15, 1996

High price per year. * 1996 as of September 30, 1996

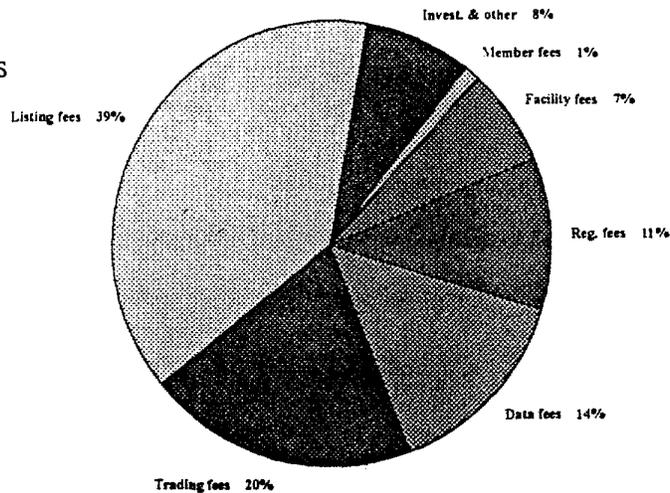
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NYSE revenues



- Main revenue sources
 - listing fees
 - trading fees
 - market data fees

1995 Revenues Total Revenues \$500 Million



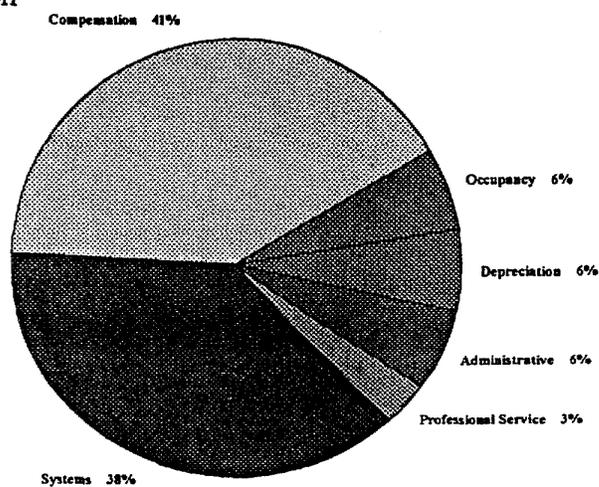
Source: NYSE 1995 Annual Report, p. 31

NYSE expenses



- Main expenses
 - employee compensation
 - systems

1995 Expenses Total Expenses: \$452 Million



Source: NYSE 1995 Annual Report, p. 31

Competition for listings



NYSE listing requirements

Minimum standards	U.S. companies	Non-U.S. companies*
Round-lot shareholders	2,000 in U.S.	5,000 global
Public shares (million)	1.1 in U.S.	2.5 global
Market value (\$ million)	40 in U.S.	100 global

* Non-U.S. companies can use U.S. or non-U.S. standards

NYSE listing fees

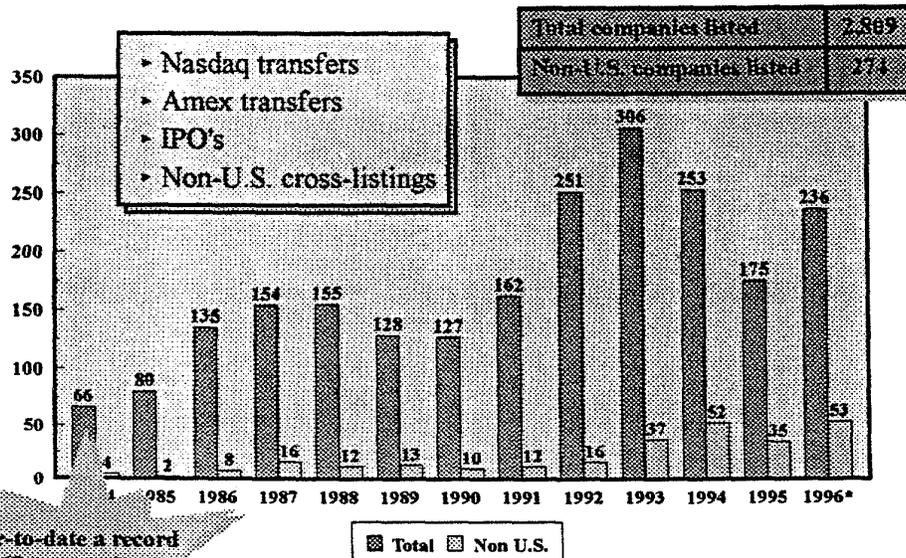
U.S. company with 4 million shares	\$
Original fee	81,100
Annual fee	16,170

U.S. prospects	650
Non-U.S. prospects	2,300

Non-listed companies meeting listing requirements

Figures as of September 30, 1996

Adding companies to the NYSE list



Year-to-date a record
69 companies
transferred from
Nasdaq to the NYSE

* Through September 30, annualized (total 177, non-U.S. 40)
Information on Nasdaq transfers from USA Today, October 22.

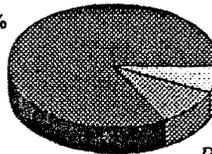
95

Unlisted trading privileges (UTP) listing at one allows NYSE to trade only listed stock trading anywhere

Competition for order flow



NYSE 83%



- NYSE stocks trade in several markets

- NYSE, the dominant market
- regional exchanges
- OTC

OTC 7%
Regional 10%

1995 Share Volume

- Also

- crossing networks and other proprietary trading systems
- overseas

Intermarket Trading System (ITS)

- an electronic communications network
- links participating U.S. exchanges and OTC market
- facilitates the execution of orders at the best ITS quote
- quote matching is allowed

from other markets

order need not be displayed by the specialist

at C-mediated integration (CIS), regional exchanges match best price or move order to specialist

The NYSE trading floor



- Specialists

- Floor brokers

- Floor officials

- supervise the trading process

\$125 million technology plan

- re-engineering of the trading floor
- new electronic display books
- flat panel screens
- cellular phones
- hand-held broker terminals
- new broker booth system
- current capacity to handle 2 billion share days being expanded to 4 billion shares

ARIZONA Stock Exchange is not a reg. exchange but a ITS

do not report to NYSE and volumes are met through crossing network. 3rd market is 25% of NASDAQ.

Proprietary trading systems set up by brokerage firms for institutional trades + 3rd market. are bench mark

Specialists



- **At the center of the order flow are the NYSE specialists**
 - each stock is assigned to a specialist firm
 - specialists act as brokers arranging trades
 - occasionally act as dealers
- **Specialist obligations**
 - continuously post prices at which investors can trade
 - manage the order flow
 - stabilize prices

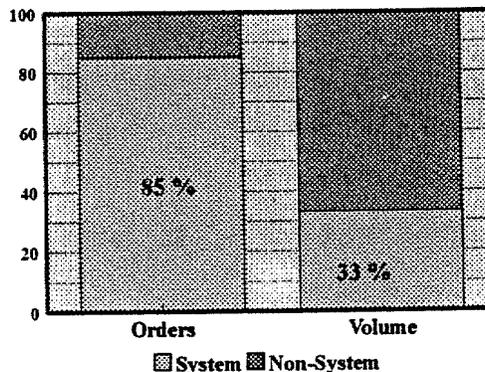
Specialist units	37
Full-time specialists	451

Figures as of September 30, 1996

Order transmission



- **Most orders reach the floor electronically via SuperDot**
 - system orders
- **Member firm to**
 - specialist workstation
 - broker booth workstation



- **SuperDot transmits execution reports back to firm**
 - market order average turnaround time is 22 seconds

Figures are for 1995

91

Floor brokers



- **Some orders reach the specialist through floor brokers**
 - by phone to broker booth
 - by SuperDot to broker booth
 - floor broker walks order to specialist post
- **Why use a floor broker?**
 - no dealer trading so no danger of front-running
 - large orders benefit from strategic behavior

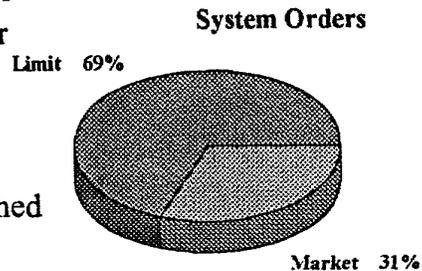
Floor brokers	906
Independent (two dollar) brokers	534

Figures as of July 18, 1996

Types of orders



- **21 different types of orders**
- **Market orders**
 - execute immediately at the posted quote or better
 - buy orders execute at the ask or better
 - sell orders execute at the bid or better
 - liquidity users, pay the spread
- **Limit orders**
 - execute at a specified price or better
 - will execute only if that price is reached
 - liquidity suppliers, save the spread
 - limit orders usually make the quote



Figures for 1996 first quarter

Order execution



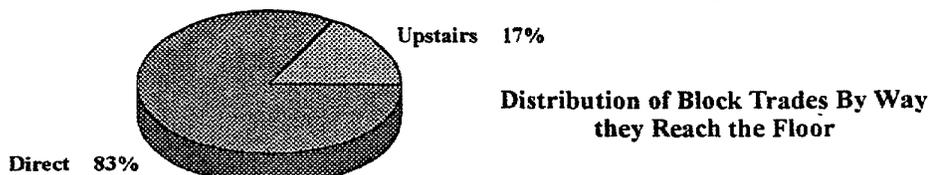
- A market order to sell 1,000 shares reaches the specialist
- Who buys the 1,000 shares?
 - public *limit orders* in the electronic display book
 - floor brokers in the *crowd* for their clients
 - the NYSE specialist
 - specialists or limit orders at regional exchanges via ITS
 - OTC dealers via ITS



Large orders and the Upstairs Market



- Some large orders reach the floor through the upstairs market
 - upstairs dealers seek counterparties
 - minimize price impact
- Once matched upstairs, floor brokers cross these orders on the floor according to NYSE rules
 - the upstairs market is integrated with the floor
 - upstairs dealers use floor prices to match large orders

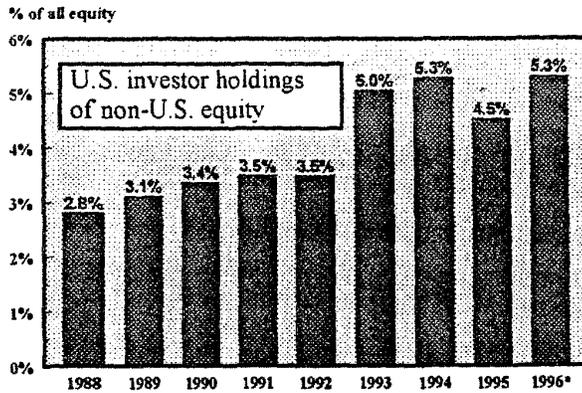


Block trades in DJIA stocks, January 1994

Globalization of equity markets



- **Non-U.S. corporations are increasingly raising capital outside their home base**
 - massive privatization programs
 - not enough capital in home country
- **U.S. investors are increasing their holdings of non-U.S. equity**
 - trend will continue



U.S. investor holdings went up from less than 3% in 1988 to almost 6% now



Source: Federal Reserve Board "Flow of Funds;" * Second quarter 1996

U.S. investor access to non-U.S. equity

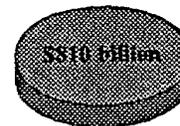


- **Through non-U.S. markets**
 - buy Japanese stocks in Japan
 - buy German stocks in London



1995

- **Through U.S. markets**
 - buy non-U.S. stocks on NYSE, AMEX, Nasdaq, Bulletin Board, Pink Sheets



- **Open-end funds**
- **Closed-end country funds**
- **Global equity index derivatives**

Source: Baring Securities International; figures are for 1995; * estimates

NYSE non-U.S. stocks



Five most actively traded

	Country	Daily volume (\$ million)
Telebras	Brazil	113
Royal Dutch Petroleum	Netherlands	112
Telefonos de Mexico	Mexico	93
Schlumberger	Neth. Antilles	61
British Petroleum	U.K.	54
Overall NYSE average		5

	Number of issues	Daily volume by country (\$ million)
U.K.	57	274
Canada	59	262
Netherlands	11	192
Mexico	28	142
Brazil	2	116

Top five countries by trading volume

Figures are for 1996 through September 30; consolidated

Cross-listings and the cost of capital



- **Positive price impact of listing**
 - up to 10% relative to appropriate benchmarks
- **Why?**
 - increased liquidity
 - increased shareholder base
 - reduced exposure to domestic market risk
 - reduced capital flow barriers
- **The result**
 - reduced cost of capital

Non-U.S. companies lower their cost of equity capital by cross-listing on the NYSE

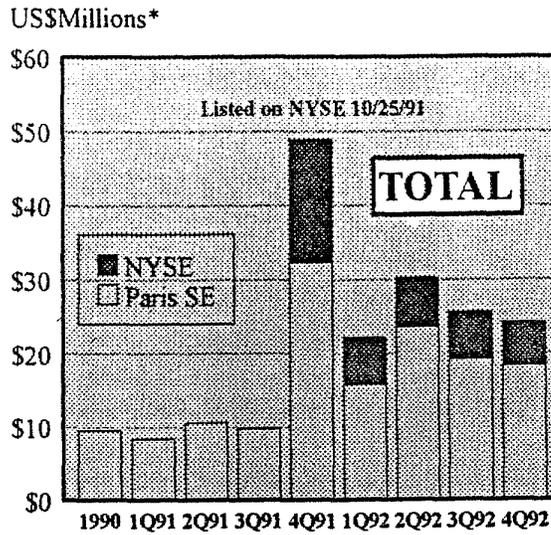
Source: Sundaran and Logue. "Valuation Effects of Foreign Company Listings on U.S. Exchanges," *Journal of International Business Studies*, 1996.

Foerster and Karolyi. "The Effects of Market Segmentation and Illiquidity of Asset Prices: Evidence from Foreign Stock Listing in the US." Working Paper, University of Western Ontario.

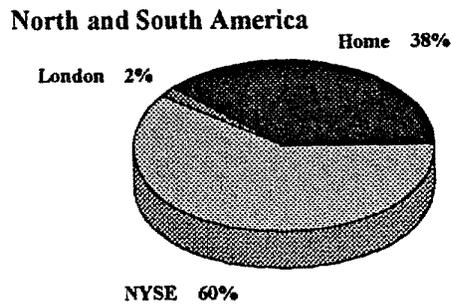
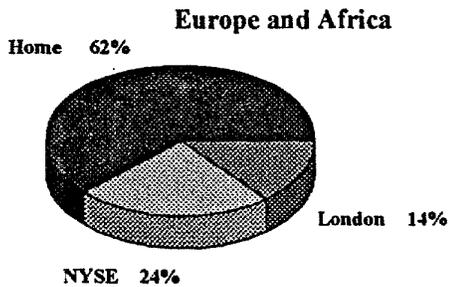
The size of the global trading pie



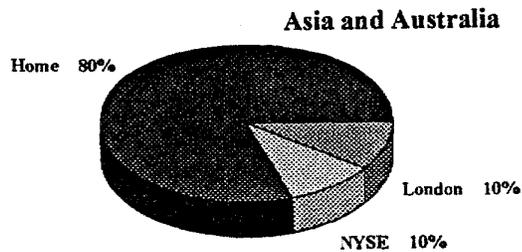
- Combined trading increases following cross-listing
 - not a zero-sum game
 - home market gains



Slicing up the pie: U.S. trading of non-U.S. stocks



- Factors affecting U.S. trading of non-U.S. stocks:**
- time zone of company's home base
 - cross-border capital raising
 - characteristics of home market
 - company-specific characteristics



10%



The world puts its stock in us.SM

Constitution and Rules

June 1996

The Official Constitution and Rules of the
New York Stock Exchange, Inc. 11 Wall Street,
New York, NY 10005.

	Page
Constitution	1011
General Rules	2501
Dealings and Settlements	2601
Admission of Members Allied Members and Member Organizations	3001
Operation of Member Organizations	3501
Communications with the Public	4001
Disciplinary Rules	4051
Listing and Delisting of Securities	4201
Arbitration	4301
Option Rules	4501
Exchange Stock Portfolio Rules	4801
Off-Hours Trading Facility Rules	5101
Index to Constitution and Rules	5501

Cross-references in the text to paragraph numbers
above 14000 refer to other sections of the full
New York Stock Exchange Guide.

A Telephone Director to Exchange departments
and personnel and a list of Exchange Services
start on page 901 in Volume 1 of the New York
Stock Exchange Guide.



CCH INCORPORATED
Chicago

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ARTICLE IV

Board of Directors

¶ 1151

Powers of Board

SEC. 1. *Powers of Board.* The Board shall be vested with all powers necessary for the government of the Exchange, the regulation of the business conduct of members, allied members and member organizations of the Exchange and of approved persons in connection with their conduct of the business of member organizations and the promotion of the welfare, objects and purposes of the Exchange and in the exercise of such powers may adopt such rules, issue such orders and directions and make such decisions as it may deem appropriate.

The Board may prescribe and impose penalties for the violation of rules adopted pursuant to this Constitution and for neglect or refusal to comply with orders, directions or decisions of the Board or for any offense against the Exchange, the penalty for which is not specifically prescribed by this Constitution.

Each person elected to the Board who is not a member of the Exchange shall have the right to go upon the Floor of the Exchange but shall not have the right to transact business thereon.

¶ 1152

Composition of Board

SEC. 2. *Composition of Board.* The Board shall consist of twenty-four directors elected by the members of the Exchange, a Chairman of the Board, the Executive Vice Chairman, if there be one, and the President, if there be one. The directors elected by the members shall consist of twelve public directors and twelve industry directors. The directors elected by the members of the Exchange shall be divided into two classes of twelve each (sometimes referred to as class A and class B) whose terms of office shall expire in alternate years. Each class shall consist of six public directors and six industry directors.

(a) the public directors shall include the following:

(i) at least one of the public directors shall be associated with a corporation that is not a financial institution and is the issuer of securities that are admitted to dealings upon the Exchange, and

(ii) at least one of the public directors shall be associated with a financial institution that is a significant investor in equity securities.

(b) the industry directors shall include the following:

(i) two of the industry directors in class A and three of the industry directors in class B shall be associated with member organizations that engage in a business

involving substantial direct contact with securities customers and shall reside and have their principal places of business within the metropolitan area of New York City, and

(ii) one of the industry directors of each class shall be associated with a member organization that engages in a business involving substantial direct contact with securities customers and shall reside and have his or her principal place of business outside the metropolitan area of New York City, and

(iii) one of the industry directors in class A and two of the industry directors in class B shall be registered as specialists and shall spend a substantial part of their time on the floor of the Exchange, and

(iv) one of the industry directors in class A shall be associated with a member organization that has its principal place of business in the metropolitan area of New York City, is not national in nature and is not engaged in activities as a specialist, and

(v) one of the industry directors in class A shall spend a majority of his or her time on the floor of the Exchange, shall have as a substantial part of his or her business the execution of transactions on the floor of the Exchange for other than his or her own account or for the account of his or her member organization, but shall not be registered as a specialist.

No person who has been elected a director by the membership to three consecutive terms shall be eligible for election as a director except after an interval of at least two years.

Each person who is not a member of the Exchange and is elected to the Board shall, by the acceptance of the position of director, be deemed to have agreed to uphold this Constitution.

¶ 1153

Meetings of Board

SEC. 3. *Meetings of Board.* Meetings of the Board shall be held at the Exchange's principal office in the state of New York or at such other place, within or without such state, as the Board may from time to time determine or as shall be specified in the notice of any such meeting. The Board shall meet for the purpose of organization, the election of officers and the transaction of other business, on the same day the annual meeting of members is held. Notice of such meeting need not be given. Special meetings of the Board may be called by the Chairman of the Board or pursuant to the written request of four directors upon notice as below prescribed.

¶ 1154

Notice of Board Meetings

SEC. 4. *Notice of Board Meetings.* Notice of a meeting of the Board shall be given by the Secretary of the Exchange or by a person calling the meeting to each director, other than any who have duly waived notice, by written notice mailed first class postage prepaid, not later than five business days before the meeting, or by electronic communication. Any notice shall be sufficient if addressed to a director at his or her office or at such other address as he or she shall have requested the Secretary of the Exchange to direct notices.

¶ 1155

Quorum at Board Meetings

SEC. 5. *Quorum at Board Meetings.* A majority of the entire Board shall be present in person at any meeting of the Board in order to constitute a quorum for the transaction of business at such meeting. Participation in a meeting by means of a conference telephone or similar communications equipment allowing all persons participating in the meeting to hear each other at the same time shall constitute presence in person at a meeting. Except as otherwise expressly required by law or the certificate of incorporation of the Exchange or this Constitution, the act of a majority of the directors present at any meeting at which a quorum is present shall be the act of the Board.

[The next page is 1063-3.]

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the absence of a quorum at any meeting of the Board, a majority of the directors present may adjourn such meeting from time to time until a quorum shall be present. Notice of any adjourned meeting shall be promptly given. At any adjourned meeting at which a quorum is present, any business may be transacted which might have been transacted at the meeting as originally called. The directors shall act only as a Board and the individual Directors shall have no power as such.

¶ 1156 **Organization Meeting**

SEC. 6. *Organization Meeting.* At its organization meeting the Board, by the affirmative vote of a majority of the entire Board, shall elect the Chairman of the Board and, from among the industry directors, one or more Vice Chairmen of the Board as the Board may deem appropriate, such Chairman and each such Vice Chairman to serve until the next organization meeting of the Board and until their successors have been elected and take office. At its organization meeting, the Board in its discretion may also, by the affirmative vote of a majority of the entire Board, elect an Executive Vice Chairman of the Board to serve for such period as the Board shall determine. The Board, at its organization meeting, shall by the affirmative vote of the entire Board, designate the person or persons to serve in the absence, inability to act or vacancy in the office of the Chairman of the Board.

¶ 1157 **Resignation of Directors**

SEC. 7. *Resignation of Directors.* Any director may resign at any time by giving written notice of resignation to the Board or the Chairman of the Board or the Secretary of the Exchange. Any such resignation shall take effect at the time specified therein, or, if the time when it shall become effective shall not be so specified, then it shall take effect immediately upon its receipt.

¶ 1158 **Vacancies**

SEC. 8. *Vacancies.* Any vacancy in the office of a director of any class elected by the membership shall be filled by the affirmative vote of a majority of the entire Board, unless the Board shall determine that the vacancy need not be filled until the next annual election. Prior to filling such vacancy, the Board shall request the Nominating Committee to submit to the Board the name of the person recommended by the Nominating Committee to fill such vacancy. Any person to be eligible to fill such vacancy must meet the qualifications for election in the class of directors in which the vacancy exists, so that upon his or her election the composition of that class shall meet the requirements of this Article. A director so elected shall serve until the next annual election of the Exchange and until his or her successor is elected and takes office.

¶ 1159 **Loss of Qualification**

SEC. 9. *Loss of Qualification.* If the Board shall determine by the affirmative vote of a majority of the entire Board that any director has lost any qualification needed for office, such person shall cease to be a director and his or her office shall become vacant.

¶ 1160 **Action by Written Consent**

SEC. 10. *Action by Written Consent.* Any action required or permitted to be taken by the Board or any committee thereof may be taken without a meeting if all members of the Board or the committee unanimously consent in writing to the adoption of a resolution authorizing the action.

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¶ 1161

Fees and Compensation

SEC. 11. *Fees and Compensation.* By the affirmative vote of a majority of the entire Board, the Board may fix the fees and compensation to be paid to the directors, members of such committees as it may from time to time authorize, the Chairman of the Board, other officers of the Exchange, arbitrators and the trustees of the Gratuity Fund.

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¶ 1162 Failure to Discharge Duties

SEC. 12. *Failure to Discharge Duties.* In the event of the refusal or failure of a director of the Exchange, or a trustee of the Gratuity Fund, to discharge his or her duties, or for any cause deemed sufficient by the Board, the Board may, by the affirmative vote of a majority of the entire Board, remove any such director or trustee and declare that office or position to be vacant.

¶ 1163 Interpretation of Constitution and Rules

SEC. 13. *Interpretation of Constitution and Rules.* The Board shall have power to interpret this Constitution and all rules adopted pursuant hereto. Any interpretation made by it shall be final and conclusive.

¶ 1164 Delegation

SEC. 14. *Delegation.* The Board may delegate such of its powers as it may from time to time determine, subject to the provisions of this Constitution and applicable law, to such officers and employees of the Exchange, and to such committees, composed either of directors or otherwise, as the Board may from time to time authorize; provided, however, that a member, member organization, allied member or approved person affected by a decision of any officer, employee or committee acting under powers delegated by the Board may require a review by the Board of such decision, by filing with the Secretary of the Exchange a written demand therefor within 10 days after the decision has been rendered, except as otherwise provided in Article IX or the rules thereunder.

¶ 1165 Conflict of Interest

SEC. 15. *Conflict of Interest.* No director shall participate in the adjudication of any matter in which he or she is personally interested.

Amendments.

November 22, 1988.

ARTICLE V***Nominating Committee*****¶ 1201 Composition, Organization Meeting and Eligibility**

SEC. 1. *Composition, Organization Meeting and Eligibility.* The Nominating Committee shall be composed of:

- (a) Four persons who would, were they directors, satisfy the definition of public director; and
- (b) Four persons who would, were they directors, satisfy the definition of industry director.

The members of the Nominating Committee shall be divided into two classes of four each whose terms of office shall expire in alternate years. Each class shall consist of two persons described in (a) above, and two persons described in (b) above.

On the first Monday after the annual election of the Exchange, or as soon thereafter as may be practicable, the members of the Nominating Committee, by the affirmative vote of a majority of such members, shall elect a chairman who shall be a member of the Nominating Committee and who shall serve until the next annual meeting of the Nominating Committee and until his or her successor is elected and takes office. The chairman of the Nominating Committee shall not succeed himself or herself as chairman and the office of chairman shall alternate from year to year between a member of the Nominating Committee described in (a) above and a member of the Nominating Committee described in (b) above.

No director shall be eligible to serve on the Nominating Committee. No member of the Nominating Committee who has served the full term for which he or she was elected by the membership shall be eligible for reelection to the Nominating Committee in the year during which such term expires. No member of the Nominating Committee who has been elected to fill a vacancy in the Nominating Committee shall be eligible for reelection to the Nominating Committee in the year during which the term of the member being replaced expires. Any vacancy in the Nominating Committee shall be filled by the remaining members thereof, who shall elect a person qualified to fill the vacancy who shall serve until the next annual election of the Exchange and until his or her successor is elected and takes office. The Board shall have no control over or power with respect to the Nominating Committee. Nothing in this Section is to be construed to prevent the Nominating Committee from soliciting the views of the Chairman or other members of the Board.

¶ 1202**Public Meetings**

SEC. 2. *Public Meetings.* The Nominating Committee shall hold one or more meetings, to which all members and allied members shall be invited for the purpose of suggesting nominees for the offices and positions to be filled at the annual election of the Exchange. The Nominating Committee shall report to the Secretary of the Exchange, not later than the second Monday in March, nominees for such offices and positions. Each nominee shall be a person who, in the opinion of the Nominating Committee, is eligible for election to the office or position for which he or she is nominated. The Secretary of the Exchange shall, on receipt of the report of the Nominating Committee, notify the members of the Exchange of the names of such

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nominees. The Chairman of the Board shall serve in a consultative role to the Nominating Committee. In that capacity the Chairman of the Board shall meet with the Nominating Committee prior to March 1 of each year to report on the needs of the Board and to provide any other information relevant to the work of the Nominating Committee.

¶ 1203**Nominees by Petition**

SEC. 3. *Nominees by Petition.* Members of the Exchange may propose by petition nominees for the offices or positions to be filled at the elections prescribed by this Constitution. Any such nominee must be endorsed by not less than forty members and no member shall endorse more than one nominee, provided, however, that one hundred members may, by petition, propose an entire ticket or any portion thereof. The petitions shall be filed with the Secretary of the Exchange in sealed envelopes within two weeks after the date fixed for the report of the Nominating Committee. The Nominating Committee and the Secretary of the Exchange shall open such envelopes and shall report to the Board the names of the persons nominated by petition who, if found eligible for election by the Board, shall be deemed nominees for such offices or positions.

¶ 1204**Names of Nominees**

SEC. 4. *Names of Nominees.* The names of all nominees shall be arranged on the ballot in alphabetical order for each class of office or position and shall be reported to the Exchange promptly after the Board shall have passed upon the eligibility of the persons nominated by petition. The names of the persons nominated by the Nominating Committee shall be identified by an appropriate legend or symbol.

¶ 1205**Death of Nominee**

SEC. 5. *Death, etc., of Nominee.* In case of the death, withdrawal, disqualification or failure to qualify, at any time in advance of the annual election, of any nominee for one of the offices or positions to be filled at such annual election, the election of a person to fill such office or position shall not be held at the annual meeting of the members of the Exchange, but this shall not delay the election of persons to fill all other offices or positions. The Board, by the affirmative vote of a majority of the entire Board, thereupon may declare such office or position vacant and if the election for such office or position was not contested may elect a person to fill the vacancy to hold office until the annual election of the Exchange in the succeeding year. Prior to filling such vacancy, the Board shall request the Nominating Committee to submit to the Board the name of the person recommended by the Nominating Committee to fill such vacancy. If such election was contested, the Board shall direct that such office or position be filled by vote of the members of the Exchange entitled to vote thereon at a special meeting of the members. If such special meeting shall be directed, the Board shall call the meeting and determine the procedure for nominations and voting by proxy at the meeting.

¶ 1206**Selection of Nominees**

SEC. 6. *Selection of Nominees.* The Nominating Committee in seeking nominees for all offices and positions shall propose persons who, in the opinion of the Nominating Committee, are committed to serving the interests of the public and strengthening the Exchange as a public securities market.

In selecting nominees who are to be members of the Nominating Committee, the Nominating Committee should consider representatives from all Exchange constituencies, taking care to avoid having an undue concentration of such nominees from any one area or industry.

In seeking nominees who are to be public directors, the Nominating Committee should consider, among others, representatives of corporations, the securities of which

are admitted to dealings upon the Exchange and representatives of financial institutions, such as investment companies, banks and trust companies, and insurance companies, which are significant investors in equity securities, care being taken to avoid having an undue concentration of such nominees from any one area or industry.

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Attachment H.

Chicago Stock Exchange- Rules for Co-specialists

Added Mar. 7, 1980; amended Nov. 2, 1984, Feb. 12, 1985, May 12, 1987

.02 CO-SPECIALIST JOB DESCRIPTION.

I. General

An Exchange member who is registered as a co-specialist is accountable to the Exchange and the investing public for the quality of the Exchange markets in the securities in which he is registered and is responsible for fostering and acting to maintain liquid and continuous two-sided auction markets on the Exchange Floor in those securities. This is accomplished by his acting as agent and principal in such securities, in accordance with the provisions of Federal and Exchange rules and policies, to help insure that such markets are fair, orderly and operationally efficient in the public interest, and competitive with non-Exchange markets in those securities. A "fair" market is one which is free from manipulative and deceptive practices and which affords no undue advantage to any of the participants therein. An "orderly" market is one with regularity and reliability of operation manifested by the presence of price continuity and depth exhibited by the avoidance of large and unreasonable price variations between consecutive sales on the consolidated tape for Dual Trading System issues, on the Exchange tape for exchange issues, and on the NASDAQ System for Nasdaq/NM Securities and the avoidance of overall price movements, without appropriate accompanying volume.

A co-specialist's continuing registration in the securities in which he is registered is dependent upon his satisfactory performance of his responsibilities as a co-specialist as defined in Federal and Exchange rules, interpretations, releases and notices, this job description, the Code of Acceptable Business Practice for co-specialists, and the rules and practices for trading on the Exchange. A co-specialist's registration, in one or more of the securities in which he is registered, may be suspended or terminated by the Committee on Specialist Assignment and Evaluation upon a determination that he has not satisfactorily performed his responsibilities as a co-specialist. A determination by the Committee on Specialist Assignment and Evaluation to suspend or terminate a co-specialist's registration may be based on answers by floor members to questionnaires sent out by the Committee and shall be made in accordance with rules of the Exchange establishing fair procedures.

II. Principal Duties

A. As Agent

1. To act as agent on behalf of orders entrusted to him, to hold the interests of such orders above his own interest and to fulfill in a professional manner all other duties of an agent to include, but not be limited to, insuring that each such order, regardless of its size or source, receives proper representation and timely, best possible execution in accordance with the terms of the order and the rules and policies of the Exchange.

2. To act as a catalyst in the markets for the securities in which he is registered by professionally and impartially servicing the interests of other members, to be helpful, communicative, cooperative and professional, to make reasonable efforts to bring together buyers and sellers without interfering as principal unless reasonably necessary to the performance of his duties, and to act together

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- a. Reflect the depth of the current market, to the extent his agency responsibility allows, to any reasonable member inquiry.
- b. Provide market information to members in a professional and courteous manner without discrimination.
- c. Make every reasonable attempt to bring together known buyers and sellers.
- d. Given a reasonable time frame and lack of substantive change in market conditions, refrain from interfering with a cross when he has previously indicated "no interest."
- e. Refrain from interfering with a "clean" agency cross unless his bid or offer has been previously solicited; or unless the reasonably anticipated needs of the market require him to do so in order to be able to fulfill his market maintenance responsibilities, and a Floor Procedure Committee member has been consulted in the event of any disagreement.
- f. Insure that in his absence, his post is properly staffed by his registered relief co-specialist.

4. Stop Orders.

When co-specialist has been entrusted as broker with a stop order, he should insure, consistent with current market conditions, that its election results from the fair and orderly price movement of the stock and does not result from poor performance or inadequate depth.

5. Operating Practices.

In view of his central position in the Exchange's marketplace, a co-specialist's operating practices can have a significant impact on the competitiveness of the market. Therefore, a co-specialist should:

- a. Report executions of orders entrusted to him in a timely and adequate manner.
- b. Maintain necessary manpower and supervision of staff to insure the efficiency of his co-specialist operations.
- c. Readily provide records when necessary to research the status of an order or a questioned trade.
- d. Cooperate with other members in the resolution and adjustment of errors.
- e. Cooperate in the implementation and operation of new Exchange procedures and systems.
- f. Cooperate in the resolution of inquiries and complaints which relate to the stocks in which he is registered.

Amended May 4, 1988; Aug. 15, 1996.

¶ 1922

Precedence to Orders in Book

RULE 2. The specialist, co-specialist and relief specialist shall at all times give precedence to orders in the book for purchase or sale of securities over the orders which originate with him or it as a dealer, provided, his or its orders and those of his or its customer are market orders, or limited orders at the same price. Notwithstanding the foregoing, whenever a specialist, co-specialist or relief specialist elects to accept a

[The next page is 2213-3.]

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all aspects of his job. Failure to do so can be detrimental to the Exchange and constitutes a breach of public trust.

While the co-specialist is required to act in accordance with the specific rules and policies which govern his activities, he should definitely avoid actions which are not in keeping with the spirit and intent of those rules and policies or not in accordance with high standards of business and ethical conduct. This duty is formalized by the Exchange's Rule 7 of Article VIII which states that "No member or member organization or partner, officer, director or registered employee of a member organization shall engage in conduct or proceeding inconsistent with just and equitable principles of trade."

This Code, of which the specific items set forth below are a part, has been adopted to minimize possible misconceptions as to what constitute good business practices for co-specialists and to guide the co-specialist in the performance of his duties. Certain specific areas of concern are enumerated below. This list may be modified from time to time as circumstances require. This is not to be construed as a complete list of acceptable business practices, and in circumstances not specifically addressed below, the co-specialist should be guided by the spirit and intent of the Code as described below.

Any violation of this Code will be subject to investigation and may lead to disciplinary or remedial action.

1. Trading Practices.

While a co-specialist is required to act in accordance with specific trading rules and policies, he should avoid practices and patterns of trading activity which are not in keeping with the spirit and intent of those rules and policies or which might interfere with the fair and orderly functioning of the Exchange's markets in the public interest. In this regard, a co-specialist should conduct his trading activities at all times in a manner which is consistent with this Code and with the duties of a specialist which are explained in the Exchange's co-specialist job description. When in doubt about the suitability of any action related to his co-specialist function, he should immediately consult with a member of the Committee on Floor Procedure.

2. Openings.

Due to the importance of the opening trade in a stock, a co-specialist should:

a. Provide accurate and complete current opening price indications and pre-opening information, such as the amount of stock paired off and the excess to buy or sell, to inquiring members.

b. For issues that the Exchange acts as the primary market, or in respect to Nasdaq/NM Securities, insure that the opening is not unduly hasty, particularly when at a price disparity from the previous close, and that the price reflects a thorough and professional assessment of market conditions at the time.

These practices should also be followed in the case of re-openings.

3. Cooperation and Communication.

In view of his central position in the Exchange's continuous trading process, a co-specialist should:

¶ 1921 Art. XXX

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when required, and to request delays in openings or trading halts when called for by unusual market conditions.

2. In order to foster a positive professional relationship between the Exchange and listed companies and to educate company representatives regarding the workings of the Exchange's market system, the co-specialist is permitted to have periodic contact with representatives of the companies whose securities he is registered as specialist provided he abides by applicable Federal or Exchange rules or guidelines with regard to such contacts.

3. To foster the efficient operation of the Exchange's market process by insuring the presence of adequate manpower (professional and clerical, full-time or relief) on the Floor at all times, by efficiently processing necessary trade documents and by cooperating in the resolution of questioned trades and errors.

4. To keep records required by Federal and Exchange rules, to report required information to the Exchange on a timely and accurate basis and to comply with all Exchange rules which govern the financing of co-specialist operations.

5. To be aware of and abide by all Federal and Exchange rules and policies governing his activities to include, but not be limited to, rules governing activities in non-speciality securities and trading activities off the Exchange Floor, and to be aware of and abide by any Exchange-developed Code of acceptable business practices for co-specialists.

6. In addition to the above, to take any other action not prohibited by Federal or Exchange rule or policy or precluded by professional judgment to foster and maintain liquid continuous two-sided markets on the Exchange floor and to insure that such markets are fair, orderly and efficient in the public interest and competitive with non-Exchange markets in action which would hinder the achievement of these objectives.

III. Eligibility Requirements

An Exchange member who desires to be registered to act as an Exchange co-specialist must:

1. Be associated with an existing or newly created specialist unit approved by the Exchange.
2. Complete an adequate training period.
3. Pass the Exchange-administered floor member examination.
4. Insure that the specialist unit with which he is to be associated meets the Exchange's specialist capital requirements.

Amended Aug. 15, 1996.

.03 CODE OF ACCEPTABLE BUSINESS PRACTICES FOR CO-SPECIALISTS.—

The co-specialist occupies the central position in the Exchange's continuous trading process. Consequently, the manner in which he performs significantly affects the efficiency, competitiveness and overall quality of the Exchange's markets, and largely determines the Exchange's success as a national securities market. In addition, the co-specialist occupies a position of public trust and should act at all times in a manner which does not violate that trust. Therefore, it is essential that the co-specialist adhere to the highest standards of business and ethical conduct in the performance of

with all members involved to insure that the equitable needs of all parties are considered.

3. To perform effectively the administrative duties with respect to orders entrusted to him as agent to include, but not be limited to, cooperating with other members in the confirmation of open orders and issuing timely and accurate status reports and execution reports.

4. To insure that his acceptance and execution of orders as agent are in compliance with applicable Federal and Exchange rules and policies; to accept as agent only those types of orders he is permitted to accept pursuant to those rules and policies, and not to accept any order for the purchase or sale of a stock in which he is registered directly from the company issuing such stock or any officer, director or controlling stockholder.

B. As Principal

1. To buy and sell securities as principal when such transactions are necessary in the public interest to minimize an actual or reasonably anticipated imbalance between supply (offers at or near the last sale price) and demand (bids at or near the last sale price) in the exchange market, and the absence of his transactions could otherwise result in an unreasonable lack of continuity and/or depth.

2. To make continuous two-sided quotations in the securities in which he is registered and buy and sell those securities in a manner that enhances the depth and liquidity of the Exchange's market in those securities and the competitiveness of the Exchange's market with markets on other Exchanges and elsewhere.

3. To make continuous two-sided quotations and effect transactions when necessary to fulfill his duties as principal, and to insure that such quotations, if acted upon, and transactions are in the public interest by being reasonably calculated to contribute to the maintenance of price continuity with reasonable depth in view of the general market, the market in the particular security and the adequacy of his total position in such security with respect to the actual or reasonably anticipated needs of the market.

4. To make such quotations and effect such transactions in accordance at all times with applicable Federal or Exchange rules and policies, to act as principal in a manner which does not upset the natural longer term forces of supply and demand, and to insure that each opening and reopening price (when the Exchange is either operating as the primary market or in respect to NASDAQ/NMS Securities) reflects a professional assessment of market conditions at the time with due consideration given to the balance of supply and demand as reflected by public orders.

5. To avoid transactions in a security as principal which are excessive in view of the market for such security. To trade as principal in a manner which reflects an awareness of his financial resources and to report to the Exchange any actual or imminent financial problems.

C. Other Duties

1. To insure the orderly functioning of the trading Crowd by exercising leadership and objectively observing trading Crowd activity and order-flow, to seek the advice and assistance of a member of the Committee on Floor Procedure

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Attachment I.

National Futures Association-

(1) Registration Requirements

(2) Study Outline for National Commodity Futures Examination and Branch Manager's Exam

WHY REGISTRATION

With certain exceptions, all persons and organizations that intend to do business as futures professionals must register under the Act. For seven major categories of applicants, Futures Commission Merchants, Introducing Brokers, Commodity Pool Operators, Commodity Trading Advisors, Associated Persons of any of the foregoing, Floor Brokers and Floor Traders, the CFTC has authorized NFA to receive and review applications and grant or deny registrations.

The primary purposes of registration are to screen an applicant's fitness to engage in business as a futures professional and to identify those individuals and organizations whose activities are subject to federal regulation. In addition, registration serves to identify those persons who, in order to conduct business as futures professionals, are also required to become Members or Associates of NFA.

Note: Individuals who are solely registered as Floor Brokers or Floor Traders are excluded from NFA membership.

THE FITNESS INQUIRY

The Act specifies certain disqualifications from registration, including many that are based on prior proceedings in which the applicant was found to have violated the law or in which the applicant was formally enjoined from engaging in certain activities. NFA performs an extensive background check to determine whether a disqualification exists. Three essential elements of the background check are the fingerprint cards collected from individuals, the questions on the application forms which require the applicant to disclose and supply detailed information concerning possible disqualifications, and a name check conducted with the Securities and Exchange Commission (SEC).

Fingerprints are sent to the Federal Bureau of Investigation (FBI) to determine if the applicant has a criminal record. To match a fingerprint card with an individual FBI file the FBI must be able to analyze the print pattern of all ten fingers. If the pattern of any one finger is not legible and the match cannot be made, the FBI will return the fingerprint card to NFA and NFA will have to delay processing until a new fingerprint card is obtained. For this reason it is very important that you have your fingerprints taken by a person properly trained in rolling fingerprints. There are a number of possible places where you may be able to obtain assistance in preparing an acceptable fingerprint card:

- Police Department.
- Sheriff's Office.
- City Hall.
- County Courthouse.
- A Bonding Company.
- NFA's Chicago Office.
- U.S. Embassy.
- Futures or Securities Exchanges.

Applicants are encouraged to submit more than one set of fingerprints with their application to avoid delays in obtaining additional sets if necessary for processing.

Registration Requirements

The disciplinary history questions require the applicant to disclose any facts about his or her background which might indicate disqualification. Applicants must supply explanations and certified copies of the actual official papers relating to "yes" answers. Two things must be kept in mind. First, willfully giving a false answer to one of the disciplinary history questions is a crime and a sufficient reason in itself for denying registration. Second, it is always in the applicant's best interest to support any "yes" answers with complete explanations and official documents. In the case of a "yes" answer, registration cannot be granted unless the nature of the potential disqualification is fully understood and supported by the appropriate documents. See sections of Form 7-R, Items 11 through 15, and Form 8-R, Items 14 through 23, for additional information.

WHO IS REQUIRED TO REGISTER

The information which follows should help you determine whether, by law, you are required to seek CFTC registration. If you have any questions as to whether you qualify for a particular exemption from registration, you should seek guidance by referring to the appropriate section of the Act or by consulting NFA registration personnel. See page 9 for registration of Foreign Entities. Requests for exemption or for "no action" opinions with respect to the applicable registration requirements should be submitted to the CFTC and a copy of any such request should be provided to NFA.

Futures Commission Merchant (FCM)

An FCM is an individual or organization which does both of the following:

- 1) Solicits or accepts orders to buy or sell futures contracts or commodity options *and*
- 2) accepts money or other assets from customers to support such orders.

Registration is required. There are no exemptions.

Introducing Broker (IB)

An IB is an individual or organization that solicits or accepts orders to buy or sell futures contracts or commodity options but does not accept money or other assets from customers to support such orders.

Registration is required unless:

- (a) You are registered as and acting in the capacity of an AP *or*
- (b) you are registered as an FCM *or*
- (c) you are registered as a CPO and only operate pools *or*
- (d) you are registered as a CTA and either solely manage accounts under powers of attorney *or* don't receive per-trade compensation.

Registration Requirements

Commodity Pool Operator (CPO)

A CPO is an individual or organization which operates or solicits funds for a commodity pool; that is, an enterprise in which funds contributed by a number of persons are combined for the purpose of trading futures contracts or commodity options, or to invest in another pool.

In general, registration is required unless:

- (a) The total gross capital contributions to all pools are less than \$200,000 *and*
- (b) there are no more than 15 participants in any one pool.

If a CPO qualifies for exemption from registration, it is required to file a written statement with the CFTC and NFA explaining why it is exempt. This written statement must also be provided to pool participants.

Commodity Trading Advisor (CTA)

A CTA is an individual or organization which, for compensation or profit, advises others as to the value of or the advisability of buying or selling futures contracts or commodity options.

Providing advice indirectly includes exercising trading authority over a customer's account as well as giving advice through written publications or other media.

Registration is required unless:

- (a) You have provided advice to 15 or fewer persons during the past 12 months and do not generally hold yourself out to the public as a CTA *or*
- (b) you are in one of a number of businesses or professions listed in the Act or are registered in another capacity and your advice is solely incidental to your principal business or profession

Associated Person (AP)

An AP is an individual who solicits orders, customers or customer funds (or who supervises persons so engaged) on behalf of an FCM, IB, CTA or CPO. An AP is, in effect, anyone who is a salesperson or who supervises salespersons for any of these categories of individuals or firms. The registration requirements apply to any person in the supervisory chain-of-command and not only to persons who directly supervise the solicitations of orders, customers or funds.

Registration is generally required unless:

- (a) You are already registered as an FCM, IB or Floor Broker *or*
- (b) you are already registered as a CPO if you are to be associated with a CPO *or*
- (c) you are already registered as a CTA if you are to be associated with a CTA *or*
- (d) you are already registered with the National Association of Securities Dealers and only act in the capacity of an AP associated with a CPO *or*

Registration Requirements

- (e) in certain instances where a firm's commodity interest activity accounts for no more than 10 percent of its annual revenue, the Chief Operating Officer, General Partner or other principal in the supervisory chain-of-command may be eligible for exemption from AP registration.

See page 11 for an explanation of Temporary Licensing for APs, page 21 for an explanation of Special Registration for Certain APs and page 24 for an explanation of Dual and Multiple Associations.

Floor Broker (FB)

An FB is an individual who purchases or sells any commodity futures or options contract on any contract market for any other person.

A registered FB need not also register as a Floor Trader in order to engage in activity as a Floor Trader.

Floor Trader (FT)

An FT is an individual who purchases or sells any commodity futures or options contract on any contract market for such individual's own account.

Foreign Entities

Foreign entities which transact business with U.S. customers in the capacity of an FCM, IB, CTA or CPO are generally required to register in the appropriate category. Foreign entities must meet the same filing requirements as domestic applicants. In addition each foreign entity must complete NFA's Foreign Firm Questionnaire and file NFA's Foreign Firm Affidavit agreeing under oath to make its books and records available for inspection by NFA and the CFTC and, except for applicants in the United Kingdom or Canada, an opinion of counsel opining that the secrecy laws of the country in which the applicant is located will not interfere with, or create an obstacle to, full inspection of the applicant's books and records by the CFTC or NFA.

Persons required to be registered as an FCM must maintain an office in the United States which is managed by an individual who resides in the U.S. and who is registered with the CFTC as an AP.

There are no special exemptions for foreign entities which transact business directly with U.S. customers in futures contracts and commodity options traded on domestic exchanges.

Registration is generally required of foreign entities which transact business directly with U.S. customers solely in futures contracts and commodity options traded on foreign exchanges unless:

- (a) You are an IB, CPO or CTA without a U.S. office and you have filed an agreement with NFA appointing an authorized U.S. agent for service of process for communications in connection with activities that would otherwise require registration *or*
- (b) you are an FCM subject to a comparable regulatory structure by a foreign regulator which has been granted an exemption by the CFTC and your name is on a list of eligible firms provided to

NFA by the foreign regulator and you have filed an agreement with NFA appointing an authorized U.S. agent for service of process for communications in connection with activities that would otherwise require registration.

REQUIRED FILINGS AND FEES

The following is a checklist of the application forms and other documents (if any) which must be submitted in order for an initial application for registration to be considered. If you are applying for registration in more than one category, you generally should not file duplicate forms, but you must pay the registration fee for each category. All registration fees should be submitted by check made payable to National Futures Association indicating on its face or in an accompanying cover letter the name of the applicant or in the case of AP registrations, the applicants for which the fee is submitted.

Note: Unless otherwise indicated, all questions on a required form must be answered. If a particular question does not apply to you, write "n.a."

■ *Futures Commission Merchant*

- A completed Form 7-R (see page 12).
- A completed Form 8-R, fingerprint card and fee of \$70 for each natural person named in Items 9a or 10 on Form 7-R or in Items 4a or 6a on Schedule D unless such person is currently registered with the CFTC in any capacity or is listed as a principal of a current CFTC registrant.
- A completed Form 8-R, fingerprint card, fee of \$70 and proof of passage of the National Commodity Futures Exam (NCFE) for each branch office manager and for each principal who is also required to be registered as an AP. Also, for each branch office manager proof of passage of the futures branch office manager examination (Series 30) or sponsorship by a broker-dealer and meeting the branch office manager requirements of either the New York Stock Exchange or the National Association of Securities Dealers, Inc.
- A completed Form 1-FR-FCM or FOCUS Report (certified audit).
- A statement describing the source of the current assets of the applicant named in Item 1 of Form 7-R combined with a representation that the applicant's capital has been contributed for the purpose of operating the business of an FCM and will continue to be used for that purpose.
- A non-refundable registration fee of \$250.

■ *Introducing Broker*

- A completed Form 7-R (see page 12).
- A completed Form 8-R, fingerprint card and fee of \$70 for each natural person named in Items 9a or 10 on Form 7-R or in Items 4a or 6a on Schedule D unless such person is currently registered with the CFTC in any capacity or is a listed principal of a current CFTC registrant.

Registration Requirements

- A completed Form 8-R, fingerprint card, fee of \$70 and proof of passage of the NCFE for each branch office manager and for each principal who is also required to be registered as an AP. Also, for each branch office manager proof of passage of the futures branch office manager examination (Series 30) or sponsorship by a broker-dealer and meeting the branch office manager requirements of either the New York Stock Exchange or the National Association of Securities Dealers, Inc.
- A completed Form 1-FR-IB or FOCUS Report (certified audit) or a completed Guarantee Agreement (Form 1-FR-IB Part B) from an FCM.
- If applying as an Independent IB (Non-guaranteed), a statement describing the source of the current assets of the applicant named in Item 1 of Form 7-R combined with a representation that the applicant's capital has been contributed for the purpose of operating the business of an IB and will continue to be used for that purpose.
- A non-refundable registration fee of \$100.
See the next page for an explanation of Temporary Licensing for Guaranteed IBs.

Associated Person

- A completed Form 8-R (see page 17).
- A completed and signed Sponsor's Certification (Sections I and J, page 7 of Form 8-R).
- A completed fingerprint card (for yourself).
- Proof that you have passed the NCFE unless you have been registered within two years prior to the application. If you have not taken the test, you should obtain an application form from NFA and send it, along with the required fee, to the National Association of Securities Dealers in order to be enrolled to take the test.
- A non-refundable registration fee of \$70.

Floor Broker / Floor Trader

- A completed Form 8-R (see page 17).
- A completed fingerprint card (for yourself).
- Proof of having been granted trading privileges on a designated contract market. Proof may be sent at a later date if not granted at the time of the application.
- A non-refundable registration fee of \$70 for each category.

Temporary Licensing for APs

If certain conditions are met, a person applying for registration as an AP (of an FCM, IB, CPO or CTA) may be granted a temporary license which enables the applicant to conduct business as an AP during the time the application for registration is being considered.

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These conditions are:

- All of the required forms, documents and fees must have been properly completed and submitted to NFA *and*
- no "yes" answers may have been given to Items 14 through 18 under Section G of Form 8-R. Normally, if all required documents are received simultaneously, a temporary license (valid for a maximum of six months) can be granted soon after the receipt of the application. The temporary license will convert automatically to a permanent registration in six months unless registration is formally granted or the temporary license is terminated before the end of that period.

Temporary Licensing for Guaranteed IBs

If certain conditions are met, an applicant for registration as an IB guaranteed by an FCM may be granted a temporary license which enables it to conduct business as an IB during the time the application for registration is being considered.

These conditions are:

- All of the required forms, documents, and fees for registration must have been properly completed and submitted to NFA,
- all of the required forms, documents, and dues for NFA membership must have been properly completed and submitted to NFA,
- FCM Certification D must have been properly completed and submitted to NFA,
- no "yes" answers may have been given to Items 14 through 18 under Section G of Form 8-R submitted for any principal, branch office manager or natural person listed on Schedule D, except those arising from a matter which has already been disclosed in connection with a previous application for a registration in any capacity, if such registration was granted, or which has already been disclosed more than 30 days previously in an amendment *and*
- no "yes" answers may have been given to Items 11 through 15 of Form 7-R submitted by the applicant.

Note: A properly completed Form 8-R must be submitted for each natural person listed in Items 9 and 10 of Form 7-R or in Items 4a and 6a on Schedule D along with a fingerprint card (unless exempt).

FORMS FOR INITIAL REGISTRATION

Form 7-R

Form 7-R must be completed by applicants for registration as an FCM or IB. The following suggestions are designed to help you avoid the types of errors or omissions which frequently result in registration delays or in the application being returned for additional or corrected information.

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Registration Requirements

ITEM 1— NAME AND ADDRESS

List the name of the person or organization which will be doing the activities which require registration. If you are doing business as an individual or as a sole proprietor, you must list your full name here. If your business is organized as a corporation or partnership or other business entity, list its official name here. The use of a P.O. Box number is not acceptable as an address.

Note: The name of an organization should not misrepresent the nature of an applicant's business; therefore, words such as "clearing," "board of trade," or "exchange" should be avoided.

ITEM 2 — NFA ID NUMBER

If you do not have an NFA ID number, write "n.a." List the business phone number of the person or organization applying for registration.

ITEM 3 — CENTRAL REGISTRATION DEPOSITORY NUMBER

Although a CRD number is optional, if the applicant has a CRD number, NFA strongly urges you to provide it to aid in identification.

ITEM 4 — OTHER NAMES

This question has to do with whether the person or organization indicated in Item 1 of this form is currently conducting business under any other name. If you check "yes," indicate any and all other names under which the person or organization is doing business. This is the place to put the business name if you are doing business as a sole proprietor and using a name other than your own (e.g., John Smith d.b.a. Smith Commodities).

ITEM 5 — LOCATION OF BUSINESS RECORDS

Be certain to provide all of the requested information and note that a P.O. Box is not acceptable as an address. This must be the address where the applicant keeps its business and other required records, not where the applicant's carrying broker keeps its records.

ITEM 6 — FORM OF ORGANIZATION

Check the appropriate form of organization of the business. The form of organization must be consistent with the name listed in Item 1.

ITEM 7 — LOCATION IN WHICH ORGANIZED

Regardless of your form of organization, this item must be answered. Sole proprietors should list the state in which their main business office is located.

ITEM 8 — REGISTRATION CONTACT PERSON

The name of a specific person must be given. That person does not necessarily have to be yourself or anyone directly affiliated with the business. For example, you might choose to have registration-related inquiries directed to your attorney or accountant.

ITEMS 9A & 9B — PRINCIPALS

Failure to completely and correctly provide the information requested in this space is the major reason for application processing delays.

Be certain to provide all requested information. Natural person principals should be listed in Item 9a with titles, and an indication whether they are holders or beneficial owners of 10 percent or more of the outstanding shares of any class of stock or have contributed 10 percent or more of the capital of the applicant. Non-natural person principals should be listed in Item 9b with addresses and telephone numbers. If an individual listed does not have an NFA ID number, be sure to indicate the date and place of birth (to distinguish among people with the same name). The following are answers to common questions.

■ ***Which Individuals and Entities Should Be Listed***

- Owners of 10 percent or more of any class of stock. If none is indicated to be in this category, the application will be assumed to be in error unless an explanation is attached. If a corporation or partnership owns 10 percent or more of the stock, the applicant must submit a list of officers and directors or general partners of that corporation or partnership, and may need to complete and submit a Schedule D as well.
- Persons who have contributed 10 percent or more of the capital, including subordinated debt. Again, if this is a corporation or partnership, the applicant must submit a list of officers and directors or general partners of that corporation or partnership, and may need to complete and submit a Schedule D as well.
- The owner of the business if it is a sole proprietorship. This should of course be the same name that appears in Item 1.
- General partners.
- Directors, even if they have no financial interest in the business.
- Officers.
- Any persons having the power, directly or indirectly, through agreement or otherwise, to exercise a controlling influence over the activities of the applicant which are subject to regulations by the CFTC.

Registration Requirements

■ Which Individuals Listed Need to File an 8-R, Fingerprints and Proof of Passage of the NCFE

- Any principal who is not currently individually registered as an AP, FB, or FT or a listed principal of a current registrant must submit a completed Form 8-R, fingerprint card and fee of \$70.
- In addition, a principal who is in the supervisory "chain of command" such as the president, managing director, general partner, managing partner or CEO must be registered as an AP even if the principal does not solicit customers or customers' orders or directly supervise persons who do. Such a principal must submit a completed Form 8-R, fingerprint card, fee of \$70 and, unless the principal has been registered within the two years previous to the filing of this application, must also file proof of passing the NCFE.

ITEM 10 — BRANCH OFFICES

Any location, other than the main business address at which the applicant employs persons engaged in activities requiring registration as an AP, is a branch office. This is true even if there is only one person at the location. If the applicant (the business entity listed in Item 1 of this form) has no branch offices, check "no."

If the applicant does have one or more branch offices, list the names of all persons who are branch office managers or who (if there is no one with the title of branch office manager) are designated to supervise the activities of a branch office. Branch office managers should be listed in Item 10 even if previously listed as a principal in Item 9a. Each branch office must have a different manager or designated supervisor.

Be certain to include the personal NFA ID number or, if the person does not have such a number, his or her date and place of birth. The address must also be given for each branch office. Do not use a P.O. Box number. Anyone listed in Item 10 should also be currently registered as an AP or FB or have applied for such registration.

Branch office managers must also meet other requirements:

- 1) By being sponsored by a broker-dealer and meeting the branch office manager requirements of either the New York Stock Exchange or the National Association of Securities Dealers, Inc. *or*
- 2) by passing the futures branch office manager examination (Series 30).

When completing Items 9a and 10, be sure to submit a complete registration Form 8-R for each individual listed who is not currently registered. This is very important as NFA cannot register the firm until all of the principals and branch office managers have been approved.

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Registration Requirements

ITEMS 11 THROUGH 15 — DISCIPLINARY HISTORY

Each question in this section must be answered. Any unanswered question will result in delaying the processing of the application. These items refer to the entity applying for registration, not the individuals listed in Items 9 and 10.

For any question to which the answer is "yes," a separate sheet(s) must be attached to the application, providing a detailed explanation along with copies of pertinent supporting documents (including copies of court records and any official documents you may have showing the nature of the charges and the disposition of the case). If you cannot obtain documents, provide a written explanation of the charges and disposition, and the jurisdiction of the body involved in the action along with an explanation of why documents cannot be obtained. Please note that the initial failure to file the relevant documents will delay the processing of your application and the continued failure to file these documents will result in the withdrawal of your application.

ITEMS 16 THROUGH 26 — NFA MEMBERSHIP APPLICATION

Items 16 through 26 are applicable only if you apply for NFA membership. See page 24 (How to Apply for Membership in NFA) for more information.

ITEM 27 — CERTIFICATION AND AGREEMENT

The Certification (Page 8 of Form 7-R) must be signed by an individual whose name appears in Item 9a. That is, by a principal of the business whose title is sole proprietor, general partner (if a partnership) or officer (if a corporation).

In addition to the required signature, be certain to print the name and title of the person signing, as well as the date.

Form 7-R Schedule D

This form must be completed for each entity listed in Item 9b of the Form 7-R that is not subject to regulation by the U.S. or any state in the Insurance, Banking or Securities industry or is not a U.S. publicly held company.

ITEM 1 — NAME

The name of the applicant must be the same as the name of the applicant in Item 1 of Form 7-R.

ITEM 2 — NFA ID NUMBER

If none has been assigned, write "none."

ITEM 3 — NAME OF PRINCIPAL

List the name and NFA ID of the entity listed in Item 9b of Form 7-R. If no ID has been assigned, write "none."

ITEMS 4A AND 4B — OWNERS OF THE PRINCIPAL

With respect to the entity listed in Item 3, list natural person principals in Item 4a and non-natural person principals in Item 4b along with all required information about non-natural person principals. Only principals that own 10 percent or more of the stock or have contributed 10 percent or more of the capital of the entity in Item 3 should be listed in Items 4a and 4b.

Note: Page 2 of Schedule D is not required 1) if at least one natural person principal is listed in Item 4a of Schedule D, or 2) if the entity listed in Item 4b of Schedule D is subject to regulation by the U.S. or any state in the Insurance, Banking or Securities industry, or is a U.S. publicly held company or 3) if the attachment submitted for the entity listed in Item 3 includes directors, officers or natural person general partners.

ITEM 5 — NAME OF THE HOLDING COMPANY

List the name and NFA ID of the entity listed in Item 4b of Schedule D. If no ID has been assigned, write "none."

ITEMS 6A AND 6B — OWNERS OF THE HOLDING COMPANY

With respect to the entity listed in Item 5, list natural person principals in Item 6a and non-natural person principals in Item 6b, along with all required information about non-natural person principals. Only principals that own 10 percent or more of the stock, or have contributed 10 percent or more of the capital of the entity in Item 5 should be listed in Items 6a and 6b.

CERTIFICATION

The name of the applicant or the applicant's organization must be the same as Item 1 of the applicant's Form 7-R. The Certification must be signed by an officer or general partner of the applicant.

In addition to the required signature, be certain to print the name and title of the person signing, as well as the date.

The Form 8-R is the basic biographical form used for individuals. This form must be completed by persons listed in Item 9a of Form 7-R or Items 4a or 6a on Schedule D, and by all persons listed in Item 10 of Form 7-R and by all persons applying for registration as an AP of an FCM or IB.

ITEM 1 — NAME AND NFA ID NUMBER

Indicate your full name in the appropriate space. If an NFA ID number has not been assigned, write "n.a."

ITEM 2 — APPLICATION CATEGORY

Check the appropriate box if you are applying for either registration or special registration as an AP, FB or FT, or if you are filing Form 8-R as a biographical supplement to Form 7-R, Item 9a or 10 or Items 4a or 6a on Schedule D. A principal is a natural person listed in Item 9a of Form 7-R. A principal of a non-natural person principal is a natural person listed in Items 4a or 6a on Schedule D. A branch office manager or designated supervisor is a person listed in Item 10 of Form 7-R.

Branch office managers must meet other requirements:

- 1) By being sponsored by a broker-dealer and meeting the branch office manager requirements of either the New York Stock Exchange or the National Association of Securities Dealers, Inc. *or*
- 2) by passing the futures branch office manager examination (Series 30).

ITEM 3 — SPONSOR NAME, NFA ID NUMBER, BRANCH ID NUMBER

Indicate the name, NFA ID, and Branch ID number of the firm with which you will be associated. If NFA ID or Branch ID are unknown, write "n.a."

Note: Item 3 does not apply to FB or FT applicants.

ITEM 4 — SPECIAL REGISTRATION

Provide all requested information including the date the Form 8-R is mailed if you are applying for special registration.

ITEMS 5 THROUGH 9A — PERSONAL HISTORY

Provide all requested information. Note that Items 6 through 9 may be provided on a separate sheet. Note also that although listing your Social Security number and CRD number is optional, if applicable, NFA strongly urges you to provide them to aid in identification.

ITEM 10 — EMPLOYMENT HISTORY ¹

Indicate in the first box on page 2 of Form 8-R the name of the firm and address of the firm's branch office at which you will be associated. (This does not apply to FB or FT applicants.) In completing this section, account for all time during the past 10 years even if there were periods when you were unemployed or in school. Any time gaps will result in a delay in processing the application. FB and FT applicants should leave the first box blank and begin at the second box of Item 10.

RESIDENTIAL HISTORY ¹

As in the previous section, there can be no time gaps. Note that the question asks where you lived starting with your current address. If

¹ When indicating time periods, be sure to include month and year.

Registration Requirements

you have lived at your current address for the past 10 years, so indicate.

EDUCATIONAL HISTORY ¹

List each college or university you attended. If you attended a college from which you did not obtain a degree, provide all other requested information and indicate "none" in the space for degree. If you did not attend college, you must indicate the last school attended.

ITEM 11 — TEST

If you are applying for registration as a sole proprietor FCM, IB or as an AP of either of the foregoing, you must provide proof that you have passed the NCFE within the last two years unless you have been registered as a sole proprietor FCM, IB, CTA, CPO or as an AP of the foregoing within the last two years or are currently registered as an FB. Completion of this section of Form 8-R does not meet the requirement of proof of passing the NCFE, which must also be submitted.

ITEMS 12 AND 13 — FB/FT BUSINESS ADDRESS AND EXCHANGE AFFILIATION

This section is to be completed by FB and FT applicants only. Applicants should state their business address. If you have a room, suite or box number, be sure to include it since this will be the mailing address used by NFA. You may use your home address.

Indicate by checking the appropriate box the exchange(s) where you have been granted membership or trading privileges or have an application pending.

Note: Completion of this item does not meet the requirement of proof of trading privileges. Proof of trading privileges from the exchange granting trading privileges must be provided before registration can be granted.

ITEMS 14 THROUGH 23 — DISCIPLINARY HISTORY

Each question in this section must be answered. Any unanswered question will result in delaying the processing of the application.

For any question to which the answer is "yes," a separate sheet(s) must be attached to the application providing a detailed explanation along with certified copies of pertinent supporting documents (such as copies of court records and any official documents you may have showing the nature of the charges and the disposition of the case). If you cannot obtain documents, provide a written explanation of the charges and disposition and the jurisdiction of the body involved in the action along with an explanation of why documents cannot be obtained. Please note that the initial failure to file the relevant documents will delay the processing of your application and the continued failure to file these documents will result in the withdrawal of your application.

¹ When indicating time periods, be sure to include month and year.

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APPLICANT'S CERTIFICATION

In order for an application to be processed, this certification must be signed by the person listed in Item 1 of Form 8-R; that is, by the person submitting the application.

Note: By signing the Certification containing the Applicant Agreement, you will become an NFA Associate if your sponsor is or becomes an NFA Member and you will be required to submit to the jurisdiction of contract markets under certain circumstances.

SPONSOR'S CERTIFICATION

Page 7 of Form 8-R, titled *Sponsor's Certification*, must be completed by the sponsor for each applicant for registration as an AP and must be submitted concurrently with the applicant's portion of the Form 8-R. It is not required for applicants submitting the Form 8-R only as a principal, FB or FT. However, if a principal is also registering as an AP, the Sponsor's Certification must be completed.

VERIFICATION OF EMPLOYMENT AND EDUCATION ¹

Unless the person applying for registration left a previous employment as an AP within the last 60 days, the past three years must be verified. There can be no time gaps; therefore, the time period with the current sponsor must also be verified. If the sponsor is unable to verify any other item, an explanation of the steps taken in attempting to make the verification must be provided. This is true even if an outside investigative service is used. If the person applying for registration left a previous employment as an AP within the last 60 days, the sponsor need only indicate that the person's last previous employer has been contacted. The sponsor remains responsible for verification for the past three years.

SPONSOR'S CERTIFICATION STATEMENT

This must be signed by an officer, general partner or sole proprietor of the registrant or entity sponsoring the AP. In addition to the required signature, the sponsor must be certain to print the name and title of the person signing, as well as the date.

Fingerprint Card

A fingerprint card must be submitted by all persons required to file a Form 8-R; that is, by all persons applying for registration as APs, FBs, FTs and by all persons named in Item 9a or 10 of Form 7-R or in Items 4a or 6a on Schedule D. FB or FT applicants who are currently approved in another category are not required to file a new fingerprint card. Fingerprint cards are referred to the FBI in connection with determination of the applicant's fitness for registration as a futures professional.

In preparing the required fingerprint card:

- Use only the card provided with the application.

¹ When indicating time periods, be sure to include month and year.

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Registration Requirements

- complete every box on the card *and*
- do not attempt do-it-yourself fingerprinting. It is highly unlikely that such prints will meet FBI requirements.

Unacceptable fingerprints will result in a delay in granting an individual or firm registration.

Special Registration

CERTAIN ASSOCIATED PERSONS

If you held a registration within the last 60 days as an AP and you wish to transfer to a new registered sponsor, filing Form 8-R containing no "yes" answers to questions 14-18, except those arising from a matter which has already been disclosed in connection with a previous application for a registration in any capacity, if such registration was granted, or which has already been disclosed more than 30 days previously in an amendment, may enable you to conduct business as an AP of the new sponsor upon mailing the completed Form 8-R, fingerprint card and fee of \$70.

FLOOR BROKERS OR FLOOR TRADERS

If you have terminated as a registered FB or FT within the last 60 days and otherwise qualify as provided by CFTC Regulation 3.11, you are eligible to obtain a temporary license effective upon mailing a properly completed Form 8-R.

Financial Reporting Requirements

All applicants for registration as an FCM and all applicants for registration as an IB (except those submitting a Guarantee Agreement from an FCM) are required to submit certain financial statements and schedules.

Specifically, they must submit an audited financial report which is not more than one year old. However, if the report is more than 45 days old, it must be accompanied by an unaudited financial report which is not more than 45 days old.

For the purpose of preparing such reports, the applicant may use Form 1-FR-FCM or Form 1-FR-IB Part A or an SEC FOCUS Report (if the applicant is registered with the SEC as a broker/dealer).

If you are required to file Form 1-FR-FCM or Form 1-FR-IB Part A (or if you elect to file an SEC FOCUS Report), refer to NFA Financial Requirements in the NFA Manual. It is suggested that you contact your accountant in advance to arrange for advice and assistance.

The audited Form 1-FR-FCM or Form 1-FR-IB Part A (or SEC FOCUS Report) must be accompanied by an auditor's opinion covering all required statements, and an auditor's Report on Internal Control.

FORM 1-FR-FCM — DETAILED FINANCIAL REPORT

This form must be filed by all persons or organizations applying for registration as an FCM.

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FORM 1-FR-IB PART A — DETAILED FINANCIAL REPORT

This part must be filed by all persons or organizations applying for registration as an Independent IB.

FORM 1-FR-IB PART B — GUARANTEE AGREEMENT

Persons or organizations that are IBs or that are applying for registration as IBs may file Part B in lieu of Part A. The Guarantee Agreement must be signed by an officer, general partner or sole proprietor of the IB and the FCM that will carry the accounts of the applicant's customers. The Agreement, in effect, obligates the FCM to assume financial and disciplinary responsibility for the performance of the IB in connection with futures and options customers. The IB has no further financial reporting obligations as long as the Guarantee Agreement remains in effect.

■ **Statement of Source of Current Assets and Representation of Purpose of Capital**

There is no prescribed form for this purpose. Simply write a letter on the firm's business stationery describing the source of its current assets and representing that its capital has been contributed for the purpose of operating the business for which you are applying for registration and will continue to be used for that purpose. The letter must be signed by a person listed in Item 9a of Form 7-R.

■ **Certification D**

All applicants for registration as an IB guaranteed by an FCM and seeking a temporary license must submit a signed and dated Certification D from the FCM stating that:

- 1) The education and employment history sections of the Form 8-R submitted by the applicant's principals and branch office managers have been verified for the preceding three years *and*
- 2) according to its knowledge, information, and belief, all of the information contained on the Form 7-R and each required Form 8-R is accurate and complete.

HOW TO CHANGE AN EXISTING REGISTRATION

■ **Form 8-T
Notice of Termination**

If you have a current pending or approved status as a principal or a branch office manager, or you are currently registered or pending as an AP of an FCM or IB and your affiliation with that sponsor has been or is being terminated, that sponsor must file a Form 8-T. NASD Form U-5 is acceptable in lieu of a Form 8-T. The sponsor filing the Form 8-T or Form U-5 must concurrently provide a copy to the person whose association has been terminated.

This is particularly important for APs moving to a different sponsor. The registration rules allow an AP to go to work for a new sponsor immediately upon mailing to NFA a properly completed Form 8-R provided that the Form 8-R is mailed within 60 days of the

Registration Requirements

termination of employment with the prior sponsor. Timely Form 8-T filings allow the widest possible availability of these special registration transfer rules and prevent needless registration delays.

A Form 8-T must be filed within 20 days of the termination of an AP, principal or branch office manager. A fee of \$100 will be charged for a termination notice received more than 20 days after the actual termination date.

Note: Question 8 must be completed to indicate each of the applicable affiliations to be terminated using the Form 8-T. Partial terminations must be reported on Form 8-T. For example, if a sponsor first terminates an individual's branch office manager status and subsequently terminates the individual's AP status, the sponsor would be required to file two Form 8-Ts, one at the time of each termination.

Form 7-W **Withdrawal of Firm** **Registration and / or** **NFA Membership**

If you are currently registered as an FCM or IB or currently are a Member of NFA, and you wish to withdraw your registration and/or membership, you must file a Form 7-W with NFA.

The withdrawal will become effective 30 days from the date NFA receives the request and required attachments unless the CFTC or NFA denies, conditions, postpones or expedites the withdrawal.

Form 3-R

PART I — CHANGES AND CORRECTIONS IN REGISTRATION INFORMATION

Use this form to report changes to any CFTC form you previously filed. For instance,

- 1) if your address changes, indicate the new address on Part I of this form and file it with NFA to effect the change to your records
or
- 2) if you are reporting changes to disciplinary history, be sure to provide certified copies of applicable documents *or*
- 3) if you are reporting a change in the form of organization of the registrant, be sure to provide a letter certifying that the newly formed organization will be liable for all obligations of the pre-existing organization which arose out of the Commodity Exchange Act or the regulations thereunder *or*
- 4) if you are reporting an addition of a principal to Item 9 on Form 7-R or on Schedule D, be sure to refer to NFA Registration Rule 208. In general, if the new principal is a natural person, such person must also submit a Form 8-R and a fingerprint card which should be attached to the Form 3-R unless such person is currently registered with the CFTC in any capacity or is a listed principal of a current CFTC registrant.

PART II — REPORTING OF DUAL AND MULTIPLE ASSOCIATIONS OF APs

If you are currently a registered AP whose registration is not subject to conditions or restrictions and you want to also be registered as an AP of another sponsor, you are eligible to use Form 3-R Part II to obtain immediate registration effective upon NFA's receipt of the properly completed Form 3-R Part II. Form 3-R Part II must be signed by an appropriate signatory of each sponsor you are currently associated with and by the additional sponsor you are becoming associated with.

ANNUAL REGISTRATION UPDATE

Any entity registered as an FCM or IB must file with NFA a Form 7-R update and appropriate fees annually on a date specified by NFA. Failure to file the Form 7-R update and appropriate fees within 30 days following such date shall be deemed to be a request for withdrawal of registration and NFA membership.

WHERE TO SEND APPLICATIONS FOR REGISTRATION

Once you have completed the necessary application forms and attached all of the required documents, they should be mailed with your registration fees to:

National Futures Association
Office of the Secretary
P.O. Box 98383
Chicago, IL 60693-0001

Note: Any filings that do not have a fee (Form 3-R, Form 8-T, Form 7-W, Form 3-R Part II) should be mailed to NFA at 200 W. Madison St., Chicago, IL, 60606.

HOW TO APPLY FOR MEMBERSHIP IN NFA

In order to conduct a futures-related business with the public, all FCMs and IBs required to be registered with the CFTC must become Members of NFA. NFA Members may not conduct customer business with any entity that is not an NFA Member unless that non-Member entity is specifically exempt from CFTC registration requirements. Persons acting as APs of NFA Members must become NFA Associates. Refer to Section H of Form 8-R for applicant agreement.

Approval of NFA membership is not automatic. Persons whose CFTC registration has been revoked or suspended (if the suspension is still in effect) may be deemed disqualified for NFA membership. So may persons who have been refused CFTC registration, persons who have been enjoined by court order from doing business as futures professionals and persons who have been convicted of a felony or certain misdemeanors. These and other grounds for denial are explained in the *NFA Manual*. See page 4008, Paragraph 4029.3, "Restrictions on Becoming or Remaining a Member or Associated with a Member."

Applicants which are denied membership have the right to appeal the denial — and, in some cases, if they request, to have a hearing before the Membership Committee — in order to demonstrate that they meet the requirements for membership. These procedures are likewise explained in the *NFA Manual* (Paragraph 4029.7).

Registration Requirements

The Membership Application

Firms or persons seeking to become NFA Members or Associates should be aware that the execution and delivery of Form 7-R and/or Form 8-R constitutes:

- 1) A representation that the information supplied in the application is complete and accurate,
- 2) an express agreement by the applicant that, if admitted to NFA membership, the applicant shall become and remain bound by all NFA requirements as are then and thereafter in effect *and*
- 3) an authorization for NFA to conduct a fitness examination and for persons contacted to release relevant information to NFA.

Application forms for NFA membership or Associate membership are incorporated in Forms 7-R and 8-R. These forms must be signed by the appropriate signatory.

Applications, along with annual dues, should be mailed to:
National Futures Association
Office of the Secretary
P.O. Box 98383
Chicago, IL 60693-0001

NFA APPLICATION TIPS

All applicants for membership should, at the outset, carefully read the instructions which accompany the application forms. The approval of applications for membership in NFA can be greatly expedited when all required forms are completely and properly prepared and are accompanied by the appropriate annual dues. All NFA dues, as well as registration fees, are non-refundable.

FCMs and IBs should include annual dues (See Membership Annual Dues Schedule on the next page) and Form 7-R, Items 16-27.

APs should include Form 8-R containing the Applicant Agreement (Item H).

While most questions and requests for information are self-explanatory, the following suggestions may be helpful in filling out forms:

- Be certain that the Applicant's Name given in Item 16 is the same as listed in Item 1 of Form 7-R.
- Items 21 and 24 of Form 7-R (pages 6 of 8 and 7 of 8) apply only to FCMs.
- If the applicant is a corporation, partnership or other business entity, the "Resolution" (Item 26) on page 7 of 8 of Form 7-R must be completed. The person in this "Resolution" must be a person who is listed in Item 9a of the applicant's Form 7-R. If the applicant is a sole proprietorship, the "Resolution" (Item 26) on page 7 of 8 of Form 7-R is not required.
- Item 25 is for membership applicants with multiple registration classes. It allows the applicant to indicate in which membership category it should be classified for Member ballot purposes (e.g., an FCM Member that is also a CTA Member).

Registration Requirements

- On page 8 of 8, "Name of Applicant or Applicant Organization" must be the same as Item 1 of the applicant's Form 7-R.
- The application must be signed by the applicant, if the applicant is an individual, or by an officer or general partner if the applicant is a corporation or partnership. In the case of a corporation or partnership this must be the person listed in the "Resolution" of the application.
- Answer all items.

NFA Annual Dues

MULTIPLE REGISTRATIONS

Applicants that are registered with the CFTC (or that have applied for CFTC registration) in more than one category are required to pay NFA annual dues in only one of those categories, the category for which the annual dues is highest regardless of principal business. For example, if a firm is registered with the CFTC as both an FCM and a CPO, it would only be required to pay NFA dues as an FCM.

MEMBERSHIP ANNUAL DUES SCHEDULE

Futures Commission Merchant (exchange member)	\$1000
Futures Commission Merchant (non-exchange member)	\$5000
Commodity Pool Operator	\$500
Commodity Trading Advisor	\$500
Introducing Broker	\$500

NFA dues are non-refundable.

POSSIBLE OTHER REGISTRATION REQUIREMENTS

Whether or not you are required to register with the CFTC, the business activities in which you engage may require that you register with the SEC and/or one or more state securities agencies. For information concerning SEC registration requirements, you or your attorney may wish to contact the SEC. Your attorney should be able to advise you regarding registration with a state securities agency, if required.



STUDY

OUTLINE

FOR THE

NATIONAL

COMMODITY

FUTURES

EXAMINATION

NFA

NATIONAL FUTURES ASSOCIATION
200 W. MADISON, CHICAGO, IL 60606

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INTRODUCTION

The following outline is intended to serve as a study aid for persons preparing for the National Commodity Futures Examination ("NCFE"). It provides an indication of the subject matter that should be concentrated upon in studying for the examination, but does not list specific test items. The outline presents those areas in which National Futures Association ("NFA") and its Educational/Testing Advisory Committee feel persons involved in opening and handling customer accounts in futures contracts and options on futures should be able to exhibit knowledge and proficiency in order to effectively serve their customers. The purpose of the NCFE is to test basic entry level knowledge of the candidate. Please note that candidates do not need to memorize information relating to the terms and conditions of particular futures contracts.

Anyone applying for registration as futures commission merchant, leverage transaction merchant, introducing broker, commodity pool operator, commodity trading advisor, or as an associated person ("AP") of any of the foregoing, must supply to NFA satisfactory evidence that they have taken and passed the NCFE. The NCFE is objective in format and contains 120 true/false and multiple choice questions. The NCFE will be presented as

one exam but is graded in two sections, one section dealing with general industry knowledge and the other concentrating on regulatory requirements. Candidates are required to pass both sections at the same sitting. Two and one half (2-1/2) hours time is allotted for completion of the examination. A minimum score of 70% on both sections of the examination is required for passing.

Upon completion of the examination, the PLATO system promptly scores and displays the candidate's exam grade on the terminal screen. Written verification of the exam results should be received by the candidate's sponsoring firm (or by the candidate) from NASD within 10 business days of the test date. It is *strongly* recommended that the candidate maintain a copy of their test results.

Passing the exam does not mean the candidate is registered as an AP. To be registered as an AP, the candidate must first file the proper forms and fees with NFA and, in most instances, be sponsored by an NFA Member firm. For more information on registration requirements, please call NFA's Information Center at 1-800-621-3570 (outside Illinois) or 1-800-572-9400 (Illinois only).

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EXAMINATION SUBJECT AREAS

The following is a general listing of the major subject areas of the examination and related topics covered. Possible reference materials are listed in the following section of this study outline.

PART 1

FUTURES TRADING THEORY AND BASIC FUNCTIONS TERMINOLOGY

A. General Theory

1. Development of futures markets
2. Futures and securities compared
 - Rights
 - Obligations
 - Transfer of ownership

B. The Futures Contract

1. Futures and forward contracts compared
2. Offset provisions
3. The clearinghouse function
 - Clearing members
 - Non-clearing members
4. Delivery provisions
 - Basis grade
 - Premiums
 - Discounts

C. The Structure of Futures Markets

1. Normal markets
 - Carrying charges
 - "Full carry" markets
2. Inverted markets
 - Supply shortages
 - Other factors

D. Hedging Theory

1. Risk reduction
 - Unhedged position
 - Effect on pricing of cash markets
2. Short hedging
 - Typical short hedgers: farmers, producers, holders of inventory
 - Effect on pricing of cash markets
3. Long hedging
 - Typical long hedgers: processors, manufacturers, exporters
 - Protection against price rise

E. Speculative Theory

1. Leverage
2. Risk
3. Market liquidity
4. Price volatility

F. General Futures Terminology

Associated Person	Floor Broker
Basis	Forward Contract
Bucketing	Introducing Broker
Carrying Charges	Inverted Market
Churning	Limit Up/Down
Clearinghouse	Lock Limit
Convergence	Long
Commodity Pool	Normal Market
Operator	Pit
Commodity Trading	Position Trader
Advisor	Retender
Deferred	Scalper
Discount	Short
Expit	Spot
Futures Commission	Variation Call
Merchant	Warehouse Receipt
First Notice Day	

G. General Options Terminology

At-The-Money	Out-Of-The-Money
Call	Premium
Conversion	Put
Delta	Spread
Exercise	Straddle
Expiration	Strangle
Grantor	Synthetic
In-The-Money	Options/Futures
Intrinsic Value	Time Value
	Writer

FUTURES MARGINS, OPTION PREMIUMS, PRICE LIMITS, FUTURES SETTLEMENTS, DELIVERY, EXERCISE, AND ASSIGNMENT

A. Margin Requirements

1. The nature of futures margin
 - Performance bond
 - Comparison with securities margin
 - Authority of exchanges to establish and revise requirements
 - Initial and maintenance requirements
 - Documentation: margin agreement, transfer of funds agreement
2. Margin calculations
 - Initial
 - Maintenance/variation
 - Effects of substantial price movement
 - Effects of change in requirements on new and existing positions
 - Withdrawal of excess equity
3. Alternative calculations
 - Hedge margin
 - Spread margin

B. Option Premiums

1. Intrinsic value
2. Time value
3. The delta
4. Premium quotations
(Note where different from underlying contract, e.g. T-Bonds and municipals)

C. Price Limits

1. Effect of limit-up/down price change
2. Expanded limits
3. Effects on margin of limit moves
4. "Lock limit"
5. "Circuit breakers"

D. Offsetting Contracts, Settlements, Delivery

1. Liquidating long and short positions
2. First notice day
3. Trading in the spot month
4. The clearinghouse role in the delivery
5. Delivery notices
6. Retenders/"stopped" notices
7. Physical delivery, warehouse receipts
8. Cash settled contracts; how settlement is computed
 - Stock indexes
 - Municipal bonds
 - Eurodollars

E. Options Exercise, Assignment, Settlement

1. Process of assignment
2. Margin requirements upon exercise
3. Final trading/exercise dates

TYPES OF ORDERS, CUSTOMER ACCOUNTS, PRICE ANALYSIS

A. Basic Characteristics and Uses of

1. Market orders
2. Stop orders
3. Stop-limit orders
4. Market-if-touched orders

B. Additional Orders

1. Good till canceled (GTC)
2. Fill-or-kill
3. "On close"
4. "One cancels the other" (OCO)

C. Technical Price Analysis

1. Charts: bar, point and figure
2. Trendlines
3. Support/resistance levels
4. Congestion areas
5. Gaps

6. Triangles: ascending and descending
7. Double tops and bottoms
8. Volume and open interest
9. "Liquidating markets"

D. Fundamental Price Analysis

1. Effects of economic or political instability
2. Supply and demand elasticity
3. U.S. agricultural policies
4. "Crop years"
5. Hog/corn ratio

E. Interest Rate Analysis

1. Yield curves: positive, inverted, flat
2. Effects of governmental policies
 - Tax policy
 - Monetary policy

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BASIC HEDGING, BASIS CALCULATIONS, HEDGING FUTURES

A. Short Hedging and Long Hedging

1. "Anticipatory hedges"
2. Long the basis/short the basis

B. The Basis

1. How determined
2. Effect of basis charge on
 - The short hedger
 - The long hedger
3. Effect on price of commodity actually delivered or purchased
 - Transportation costs
 - Variation in deliverable grades
4. The basis in financial markets
 - Short term rates vs. long term rates
 - "Implied repo rate"

C. Hedging Calculations

1. Net result of hedge
2. Net price received upon purchase or sale

Examples:

Grains	T-Notes, T-Bonds
Livestock	T-Bill, Eurodollars
Foodstuff	Municipals
Metals	Currencies
Energy	Stock indices
Lumber	

SPREADING

A. Spread Trading

1. Order execution
2. Expectations
 - Narrowing or widening basis
 - Normal or inverted market strategies

B. Common Types of Spreads

1. Carrying charge or "limited risk" spreads
 - Intra-market
 - Inter-delivery
2. Bull and bear spreads
3. Intermarket spreads

SPECULATING IN FUTURES

A. Profit/loss calculations for speculative trades (including spreads)

1. Gross profit on speculative trades; single or multiple contract positions
2. Effect of commissions on gross profits
3. Return on (margin) equity calculations

Examples:

Grains	T-Note, T-Bonds
Livestock	T-Bill, Eurodollars
Foodstuff	Municipals
Metals	Currencies
Energy	Stock indices
Lumber	

B. Trading Applications

1. Recommend appropriate speculative trades given certain economic or technical circumstances
2. Use appropriate orders both to initiate and protect position

OPTION HEDGING, SPECULATING, SPREADING

A. Option Theory

1. Long
 - Limited risk
 - Increased leverage
 - Total loss of investment (premium) possible
2. Short
 - Increased risk
 - Earn premium
 - Loss may exceed premium received

B. Option Hedge Strategies/Calculations

1. Long put as alternative to short futures hedge
2. Long call as alternative to long futures hedge
3. Allows for increased profit once breakeven point is reached

C. Option Speculative Strategies/Calculations

1. Long call as substitute for long futures
 - Risk limited to premium
 - "Breakeven point"
 - Profit and return on equity
2. Long put as substitute for short futures
 - Risk limited to premium
 - "Breakeven point"
 - Profit and return on equity
3. Long call to protect short futures (synthetic long put)
4. Long put to protect long futures (synthetic long call)
5. Long futures-short call (covered call)
6. Conversions
7. Reverse conversions (reversals)

D. Option Spread Strategies/Calculations

1. Call bull spreads
 - Spread to widen
 - Maximum profit/loss
2. Call bear spreads
 - Spread to narrow
 - Maximum profit/loss
3. Put bull spreads
 - Spread to narrow
 - Maximum profit/loss
4. Put bear spreads
 - Spread to widen
 - Maximum profit/loss
5. Calendar spreads
6. Arbitrage spreads

PART 2

REGULATIONS

A. General

1. NFA/CFTC Registrations
 - Floor broker ("FB")
 - Associated person ("AP")
 - Commodity pool operator ("CPO")
 - Commodity trading advisor ("CTA")
 - Introducing broker ("IB")
 - Futures commission merchant ("FCM")
 - Exemptions from registration
2. Futures account opening requirements
 - "Know Your Customer Rule" (NFA Rule 2-30)
 - Verbatim risk disclosure statement
 - Commodity customer agreement
 - Discretionary accounts
 - Written authorization
 - Account supervision and review
 - AP minimum experience requirement
3. Futures options account
 - Specific disclosure of strategies employed in discretionary accounts
 - Confirmation mailing requirements
4. Position reporting requirements
 - Set by CFTC or exchanges
 - Daily reports
 - Applicable to both speculators and hedgers
5. Speculative position limits
 - Maximum net long or short position specified by CFTC or exchanges
 - Bona fide hedgers' exemption

B. FCM/IB Regulations

1. Guaranteed and non-guaranteed IBs
 - Responsibilities of guarantor FCM
 - Rules for acceptance of customer funds
2. Net capital requirements
3. Quarterly and annual financial reports
4. Collection of margin deposits
5. Customer complaints
 - Options-related complaints
 - Adjustments to accounts
6. Time-stamping requirements
7. Advertising rule (NFA Rule 2-29)
8. Disclosure by FCMs and IBs required for costs associated with futures transactions

C. CPO/CTA

1. Disclosure documents
 - Upfront fees
 - Performance records
 - Disclosure statements
 - Trading program
 - Five year business background
 - Conflicts of interest
2. Records to be maintained
3. Advertising rule (NFA Rule 2-29)

D. Arbitration Procedures

E. NFA Disciplinary Procedures

1. Written complaints
2. Warning letters
3. Hearings
 - Offers to settle
 - Appeal process
4. Member responsibility actions (MRA)
5. Penalties for violators
 - Fine
 - Cease and desist order
 - Expulsion

STUDY REFERENCES

The following list includes books that may be helpful in preparing for the National Commodity Futures Examination, noted as to availability at bookstores* and/or direct from the publisher**. Although not all-inclusive, this list is representative of the types of books available for studying.

- ****Commodity Trading Manual** 1989
Chicago Board of Trade
LaSalle at Jackson
Chicago, IL 60604
- ****CTM Home Study Course Workbook** 1990
Chicago Board of Trade
LaSalle at Jackson
Chicago, IL 60604
- ***The Futures Game 2nd Ed.**
Richard J. Teweles and Frank J. Jones 1987
McGraw-Hill Book Company,
New York, NY 10020
- ****FII Futures Trading Course** 1988
Futures Industry Institute
2001 Pennsylvania Avenue
6th Floor
Washington, D.C. 20006
- ****Futures: A Personal Seminar** 1989
New York Institute of Finance
15 Columbus Circle
18th Floor
New York, NY 10133-0040
- ***Futures Market**
Daniel R. Siegel, Diane F. Siegel 1990
Dryden Press
Hinsdale, IL 60621
- ****How the Futures Market Works**
Jake Bernstein 1989
New York Institute of Finance
15 Columbus Circle
18th Floor
New York, NY 10133-0040
- ****Trading in Options on Futures**
James T. Colburn 1990
New York Institute of Finance
15 Columbus Circle
18th Floor
New York, NY 10133-0040
- ***Understanding Futures Markets**
Robert W. Kolb 1991
Kolb Publishing
Miami, FL 33155

EXCHANGE RULE-BOOKS AND MARKET LITERATURE

In addition to the official rulebooks of the exchanges, literature on trading futures, options on futures, and on individual markets, is helpful in preparing for the examination. Please contact individual exchanges in order to obtain pricing lists, publication catalogs and order forms. Various departments within each exchange may be of assistance: Public Relations, Marketing, Literature, Member Services and Education.

Chicago Board of Trade
141 West Jackson Boulevard
Chicago, Illinois 60604
(312) 435-3500

Chicago Mercantile Exchange
30 South Wacker Drive
Chicago, IL 60606
(312) 930-1000

Coffee, Sugar & Cocoa Exchange, Inc.
Four World Trade Center
New York, NY 10048
(212) 938-2800

Commodity Exchange, Inc.
Four World Trade Center
New York, NY 10048
(212) 938-2900

Kansas City Board of Trade
4800 Main Street
Kansas City, MO 64112
(816) 753-7500

MidAmerica Commodity Exchange
141 West Jackson Boulevard
Chicago, IL 60604
(312) 341-3000

Minneapolis Grain Exchange
150 Grain Exchange Building
400 South 4th Street
Minneapolis, MN 55415
(612) 338-6212

New York Cotton Exchange
Four World Trade Center
New York, NY 10048
(212) 938-2000

New York Futures Exchange
30 Broad Street
New York, NY 10004
(212) 623-4949

New York Mercantile Exchange
Four World Trade Center
New York, NY 10048
(212) 938-2222

Philadelphia Board of Trade
1900 Market Street
Philadelphia, PA 19103
(215) 496-5000

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OTHER PUBLICATIONS

NATIONAL FUTURES ASSOCIATION NFA MANUAL (SOFTBACK EDITION)

WHAT THIS MANUAL CONTAINS — This edition contains NFA's Articles of Incorporation, Bylaws, Compliance Rules, Code of Arbitration, Member Arbitration Rules, Financial Requirements and Registration Rules.

To order a copy contact NFA's Information Center at (312) 781-1410, or use 1-800-621-3570 (outside Illinois) or 1-800-572-9400 (inside Illinois)

See enclosed brochure for information on ordering other NFA publications.

THE COMMODITY FUTURES TRADING COMMISSION

NFA's relationship to the CFTC

The Commodity Futures Trading Commission ("CFTC") oversees the regulatory activities of NFA. The CFTC also retains regulatory responsibility for the futures exchanges, floor brokers and floor traders. NFA does not regulate these industry participants.

The rules and regulations of the CFTC are encompassed in the **Commodity Exchange Act as Amended and Regulations Thereunder**. Updated regularly. Current editions may be ordered directly from the publisher:

Commerce Clearing House
4025 West Peterson Avenue
Chicago, Illinois 60646
(312) 583-8500

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All Rights Reserved

EXAMINATION PROCEDURES

ENROLLMENT

The National Commodity Futures Examination is administered for NFA by the National Association of Securities Dealers, Inc. ("NASD").

The application form ("U-10" to be used by non-NASD members and "U-4" to be used by NASD members) should be completed by the applicant and sent with the \$75.00 fee payable to:

NATIONAL ASSOCIATION OF SECURITIES
DEALERS, INC.
P.O. Box 9401
Gaithersburg, MD 20898-9401
(301) 590-6500

IDENTIFICATION

In order to gain admission to a test center, a candidate must provide the center with two forms of personal identification, both of which must contain the candidate's signature. In addition, one document must contain either a picture or a physical description of the candidate. This requirement can usually be met by presentation of a driver's license, a military identification, a passport, or a similar type of official document. In situations where this identification requirement cannot be met by a candidate, the sponsoring firm should call the Examinations Section of the NASD Membership Department prior to the appointment date so that alternate arrangements can be made.

GENERAL INFORMATION

A candidate may use a pocket electronic calculator provided it has an independent power source, has no print mechanism, and has no alphabetic keys or displays.

COMPUTER- DELIVERED EXAMINATIONS

In the U.S., the examination is given at PLATO system computer terminals at more than 50 Control Data Learning Centers located in major cities. After applying for the examination, the candidate normally receives a written notice of enrollment within 10 business days and a brochure ("Your NASD Examination and the PLATO System")* of the U.S. learning centers, addresses, and telephone numbers. The candidate can then make an individual appointment for the exam at the learning center of his choice on regular business days, during normal business hours.

The brochure which the candidate receives with the notice of enrollment explains the simple procedures used in taking the exam at the computer terminal. Typing skills are not required.

*This brochure is revised quarterly (January 1st, April 1st, July 1st and October 1st). Please refer to a current issue for accurate and timely information.



PAPER AND PENCIL WRITTEN EXAMINATIONS

Persons in areas of the U.S. not reached by the PLATO System should contact the NASD to receive a schedule of examinations and to make application. Please refer to the PLATO brochure for a list of exam locations.

GENERAL INFORMATION

DATE AND TIME

Examinations are given on the first Saturday of each month.

Candidates must report to the examination center by 8:30 a.m. local time. Examinations begin promptly at 9:00 a.m. local time. No candidate will be admitted once the examination session starts.

BY APPOINTMENT ONLY

Appointments will be necessary for all candidates who wish to take these examinations. Appointments may be made by telephoning the Information Services Section of the NASD Membership Department in Rockville, Maryland at (301) 590-6500. The caller must specify the name and social security number of the candidate, the name of the firm, the series number of the examination and the test center location desired.

CANDIDATES MUST MAKE APPOINTMENTS WITH THE NASD EIGHT (8) FULL BUSINESS DAYS PRIOR TO THE EXAMINATION SESSION DESIRED AS EXAMINATION BOOKLETS ARE SENT TO EACH CENTER ON THE BASIS OF APPOINTMENTS MADE.

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FOREIGN-ADMINISTERED EXAMINATIONS

SCHEDULE OF FOREIGN EXAMINATION CENTERS

All NASD examinations are administered abroad on the third Saturday of the month.

Candidates must report to the examination center by 7:30 a.m. local time. Examinations begin promptly at 8:00 a.m. local time. No candidate will be admitted once the examination session starts.

For information contact:
NASD Membership Department
Examinations Section
9513 Key West Avenue
Rockville, MD 20850

FOREIGN APPOINTMENT REQUEST FORM

In order to request an appointment at a foreign examination center, the foreign appointment request form must be submitted to the NASD with the foreign appointment fee for each candidate. The foreign appointment request form can be obtained from the NASD. Also, you must file the appropriate application form and testing fee with the NASD. With the exception of the General Securities Registered Representative Examination (Test Series 7), a candidate may request to sit for two examinations on the same day.

Each candidate must have a valid appointment confirmation in order to be admitted to the examination center. The foreign appointment confirmation will be honored only at the location and date and for the examination(s) specified.

The foreign appointment request form and fee must be submitted to the NASD *one month* prior to the desired test date to the following address:

NASD Treasurer's Department
9513 Key West Avenue
Rockville, MD 20850

The required forms and fees must be re-submitted to the NASD in order to re-apply for the examination(s) and/or foreign appointment.

FOREIGN EXAMINATION LOCATIONS

See the PLATO brochure for locations and dates of examinations.

NOTES REGARDING FOREIGN-ADMINISTERED EXAMINATIONS

All candidates taking NASD exams overseas will be given an extra hour.

An English/Native language dictionary may be used at all foreign examination sites after approval by the proctor.

**BRANCH MANAGER EXAM - FUTURES
SERIES 30**

Study Outline

This guide is intended to be an outline of the subject areas covered by the examination and does not represent an exhaustive list of the actual test questions.

Section 1:

General

- books and records, preparation and retention
- order tickets, preparation and retention
- written option procedures
- handling of customer deposits
- NFA Compliance Rule 2-9, supervision of employees
- registration requirements - who needs to be registered, sponsor verification, NFA Bylaw 1101, AP termination notices, temporary licenses
- NFA's disciplinary process
- reportable positions
- NFA Arbitration Rules
- on-site audits of branch offices
- bona fide hedging transactions
- trading on foreign exchanges

Section 2:

CPO/CTA General

- registration requirements
- books and records to be maintained
- reports to customers
- block orders and order allocation

Section 3:

CPO/CTA Disclosure Documents

- management and incentive fees
- performance records
- how long can a CPO or CTA use a disclosure document
- conflicts of interest
- pool units purchased by principals
- business backgrounds of principals
- amendments to disclosure documents
- disclosure of disciplinary actions
- NFA/CFTC review of document before use

Section 4:

NFA Know Your Customer Rule

- client information required
- responsibility to obtain additional client information
- risk disclosures

Section 5:

Disclosure by CPOs and CTAs Required for Costs Associated with Futures Transactions

- disclosure of upfront fees and expenses
- effect of upfront fees and organization expenses on net performance

Section 6:

Disclosure by FCMs and IBs Required for Costs Associated with Futures Transactions

- explanation of fees and charges to customers

Section 7:

IB General

- accepting funds from customers
- guarantee agreements
- responsibilities of guarantor FCM
- minimum net capital requirements
- timestamping of order tickets
- books and records to be maintained

Section 8:

General Account Handling and Exchange Regulations

- Risk Disclosure Statement
- margin requirements
- stop loss orders
- preparing orders
- block orders
- proprietary accounts
- position limits and reporting requirements
- trade confirmations

Section 9:

Discretionary Account Regulation

- requirements relating to discretionary accounts
- supervision and review of discretionary accounts

Section 10:

Promotional Material (Rule 2-29)

- definition of promotional material
- standardized sales presentations
- use of a third party consulting or advertising firm
- reprints of articles from industry publications
- recordkeeping of promotional material
- past performance
- hypothetical trading results
- written procedures for promotional material
- supervisory review of promotional material

Summary of London listing requirements



London STOCK EXCHANGE

Basic conditions for listing

Requirements	Overseas company's shares (List)	GDRs	Convertible bonds with warrants	Straight bonds	MTNs
Sponsor	Yes	Listing agent – responsible to the Exchange	Listing agent	Listing agent	Listing agent
Trading record	Three years	Three years	Three years	Three years. May be waived if an issue is fully secured or guaranteed by a state or the guarantor has published audited accounts which cover at least three years	Three years. May be waived if an issue is fully secured or guaranteed by a state or the guarantor has published audited accounts which cover at least three years
Minimum size	£700,000	£700,000	£200,000	£200,000	£200,000
Share in public hands	Normally 25 per cent of each class	25 per cent of GDRs	No requirement	No requirement	No requirement
Conditions to be met for underlying shares	Secondary listed applicants must be in compliance with rules of home exchange and competent authority	Underlying shares must be traded on a regulated, regularly operating, recognised open market (ie FIBV full member or associate member or SIB approved)	Securities into which they are convertible must be listed on a regulated regularly operating, recognised open market	Not applicable	Not applicable
Accounting standards	Normally UK, USA, GAAP or IAS unless Exchange content that standards protect investor's interest	Statement of accounting principles adopted and may require notation of departures from international accounting standards, US or UK GAAP. .Not reconciliation	Statement of accounting principles adopted and may require notation of departures from international accounting standards, US or UK GAAP. Not reconciliation	Statement of accounting principles adopted and may require notation of departures from international accounting standards, US or UK GAAP. Not reconciliation	Statement of accounting principles adopted and may require notation of departures from international accounting standards, US or UK GAAP. Not reconciliation
Investor type	Retail and professional	Professional	Professional	Professional	Professional

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Attachment J

London Stock Exchange - Listing Requirements

Summary of London listing requirements



London **STOCK EXCHANGE**

Disclosure requirements

Requirements	Overseas company's shares (List)	GDRs	Convertible bonds with warrants	Straight bonds	MTNs
Financial Information	Normally three years profit and loss, balance sheets and cashflow statements and recent interims if published or more than nine months since last year end. Independently audited	Three years profit and loss, balance sheets and cashflow statements and recent interims if published or if more than nine months since last year end	Three years profit and loss, balance sheets and cashflow statements and recent interims if published or if more than nine months since last year end	Profit and loss accounts for the last three years. Balance sheet for the last two, and notes to the accounts for the last year	Profit and loss accounts for the last three years. Balance sheet for the last two, and notes to the accounts for the last year
Latest accounts	12 months before application	18 months before application (interims required if more than nine months)	18 months before application (interims required if more than nine months)	18 months before application	18 months before application
Consolidation	Must be consolidated	Consolidation not required if accounts are not consolidated	Consolidation not required if accounts are not consolidated	Consolidation not required if accounts are not consolidated	Consolidation not required if accounts are not consolidated
Working capital statement	Yes	Not required	Not required	Not required	Not required
Conditions to be met for	Secondary listed applicants	Underlying shares must be	Securities into which they.	Not applicable	Not applicable
Accountants' report	Certain circumstances – material change or qualified accounts	Text of audit report accompanying last published accounts	Text of audit report accompanying last published accounts	Text of audit report accompanying last published accounts	Text of audit report accompanying last published accounts
Capitalisation table	Yes	Yes	Yes	Yes	Yes
Information on controlling shareholders	Yes	Yes	Yes	No	No
Disclosure of directors' salaries/contracts	Total aggregate of remuneration and benefits in last year	Total aggregate of remuneration and benefits in last year	Total aggregate of remuneration and benefits in last year	No	No
Information on major shareholders	Three per cent or more of the issuers capital	Three per cent or more of the issuers capital. Or 20 per cent if primarily listed on an overseas Exchange	Yes – if over three per cent of issued capital. Or over 20 per cent if primarily listed on an overseas Exchange	No	No

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Summary of London listing requirements



London STOCK EXCHANGE

Continuing Obligations

Requirements	Overseas company's shares (List)	GDRs	Convertible bonds with warrants	Straight bonds	MTNs
Interim report	Yes – within four months of the end of the period to which it relates	Yes – within four months of the end of the period to which it relates	No requirement	No requirement	No requirement
Annual report	Within six months of the end of the period to which they relate. UK/US/IAS	Within six months of the end of the period to which they relate. Home country standards acceptable	Within six months of the end of the period to which they relate. Home country standards acceptable	Within six months of the end of the period to which they relate. Home country standards acceptable	Within six months of the end of the period to which they relate. Home country standards acceptable
Cash flow table required in annual report	Yes	No	No	No	No
Price sensitive information disclosure	Class tests, related parties detailed and general requirements	Exchange must be notified of any major new development which may lead to substantial movements in the price of the securities	Exchange must be notified of any major new development which may lead to substantial movements in the price of the securities	Exchange must be notified of any major new development which may lead to substantial movements in the price of the securities	Exchange must be notified of any major new development which may lead to substantial movements in the price of the securities
Preliminary results	Yes	No	No	No	No
Changes of directors	Yes	No	No	No	No
Changes in shareholdings of major investors	If in member state follows law of local competent authority. If non-member and holding exceeds or falls below 10, 20, 33, 50, 66 per cent announcement should be made	If in member state follows law of local competent authority. If non-member and holding exceeds or falls below 10, 20, 33, 50, 66 per cent announcement should be made	Not applicable	Not applicable	Not applicable
Purchases, redemptions and cancellations	Not applicable	Not applicable	Purchases, redemptions or cancellations which aggregate 10 per cent should be announced and for each five per cent thereafter	Purchases, redemptions or cancellations which aggregate 10 per cent should be announced and for each five per cent thereafter	Purchases, redemptions or cancellations which aggregate 10 per cent should be announced and for each five per cent thereafter
Equivalent information to be announced in London as on home exchange	Yes	Yes	Yes	Yes	Yes

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Summary of London listing requirements



London **STOCK EXCHANGE**

Other information

Requirements	Overseas company's shares (List)	GDRs	Convertible bonds with warrants	Straight bonds	MTNs
Initial exchange fees	Scale rate dependent on money raised. Half scale rate of domestic companies	£4,000	£1,500 each application for established	Maximum £4,000 6p/£1,000 money value	£1,500/application £1,500 for first issue and issues over a cumulative £50m. Maximum charge £4,000 per tranche
Annual exchange fees	Scale rate based on nominal value. Half scale rate of domestic companies	£2,000	No charge	No charge	No charge

The Investors Compensation Scheme

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golden rules for investors.

The investment watchdogs are working to protect investors. They have a wide range of powers to ensure that standards across the investment industry are as high as possible. As part of this system of investor protection, the Investors Compensation Scheme exists as the final safety net, should the worst happen and customers of an authorised investment firm lose out.

Investors, too, have a role to play in preparing themselves for the financial decisions they face. Among the best defences against negligence or fraud are knowledge and vigilance on the part of the investing public. There are steps which all investors can take to minimise the likelihood of things going wrong, or, in the event of the unavoidable failure of an investment firm, to have the right sort of evidence to help us to pay compensation.

Over the year, staff at the Investors Compensation Scheme have been drawing up a list of 'golden rules' based on the experiences of the investors whose claims we have handled. This factsheet lists the top one hundred and one tips for investors.

Take other people's 'winning formulae' with a pinch of salt ...

- Think about your plans for the future and the financial decisions you need to take.
- Discuss with your partner important investment decisions you're thinking about making. If things go wrong, they may be the ones picking up the pieces.
- Listen to other people's views but make your *own* mind up about what's right for you.
- Take with a pinch of salt other people's 'winning formulae', especially those you hear at the pub or the golf club.
- If a stranger wants to share with you an 'investment secret', ask yourself why.
- Be wary of 'get rich quick' schemes.
- When you buy a new TV you will certainly want to shop around and ask questions. So do the same when it comes to your investments - which will probably involve considerably more money.
- 'Numbers and small print are boring' is no excuse for not taking an active interest in money matters.
- Read the money pages in your newspaper.
- Pick up any free leaflets and brochures to find out about the differences and similarities of the investment products available.

If taking a financial risk worries you, should you be taking it?

- Consider how much risk you're prepared to accept. Can you afford to lose money if investments fall in value?
- You can't have it all. Generally, the higher the potential gain, the higher the risk.
- We can pay compensation should the worst happen *only* if the firm you dealt with was fully authorised. So before you meet a financial adviser, check his business credentials on the official Central Register of authorised firms (telephone: 0171 929 3652).
- Even if family and friends recommend an adviser they have all been using for years, still check the firm's business credentials carefully before you hand over your money.
- Don't trust an adviser just because he's a 'pillar of the community' or a relative.
- Visit your adviser at his offices. This can tell you a lot about the type of business he runs.

Attachment K

U.K. Investors Compensation Scheme

- Don't be afraid to ask questions. It's *your* money and you want to know where it's going.
- Honest, competent and responsible financial advisers will not be offended by you asking them probing questions and checking their credentials!

Why is this investment right for me?

- Quiz your financial adviser to check that he's working in your best interests:
Why is this investment right for me?
How can this investment pay a higher return than my building society account?
Could I lose money?
What do *you* get out of this deal?
Would I be better off keeping my money in a bank or building society?
What happens if I stop paying my premiums?
How long have you been working in financial services?
What qualifications and experience do you have giving investment advice?

Don't pretend you understand things if you don't ...

- Be honest and candid with your financial adviser so that he knows and understands your personal and financial circumstances.
- Don't let yourself be over-awed by suave manners and plush offices.
- You should feel comfortable with your financial adviser.
- Don't exaggerate your salary, pretend you understand things you don't, or lie about your age!
- All advisers have to carry out a 'fact find' about your circumstances and investment aims. Ask for your own copy to check the details are correct.
- Exotic offshore centres offering tax free investments and banking secrecy may also offer no investor protection or compensation cover if things go wrong.
- If you're carrying out investment transactions on the Internet, make absolutely certain you are dealing with a fully authorised firm.
(Central Register telephone: 0171 929 3652)
- Each time you seek advice or invest money, check your adviser is still fully authorised and that the new investment is still covered by the Investors Compensation Scheme.

Don't let yourself be persuaded against your better judgement ...

- If an investment return seems too good to be true, it probably is.
- Putting all your eggs in one basket is usually unwise. Spread your risks, so if one investment loses money you're not left high and dry.
- Remember, the most compensation we can pay if an investment firm fails is £48,000. So should you be thinking about spreading your investments across several investment firms?
- Just because all your friends have bought a particular investment doesn't mean the same investment is right for you.
- In fact, if your adviser appears to be recommending the same investment to all his clients, ask why. Ask for alternative ideas.
- It's always worthwhile getting a 'second opinion', particularly if you are investing a large sum.
- Be wary if you're offered as a 'favour' the last place in a 'special scheme' available 'only for close friends and family'.
- Bear in mind that slick marketing - free gifts and generous hospitality - is ultimately being paid for by investors.

And keep on asking until you do understand ...

- If you don't understand something, ask the firm to clarify it.
- Keep on asking until you are happy that you *do* understand.
- Remember there's no magic in technical words and jargon. 'Bonds', 'niche investment funds' and 'special investment opportunities' may sound enticing, but what exactly do they involve?
- 'Plans' can sound straightforward and common-sense. But if the plan involves a package of financial arrangements, do you fully understand how each part works and how it all fits together?
- It is very important to understand how your money is working for you.
- If you've never heard of the investment your adviser recommends, or if it seems particularly complicated, is this really what you want?
- High pressure 'hard sell' tactics are now effectively outlawed by the investment regulators.
- But bear in mind that the 'soft sell' can be just as effective at persuading you to buy something against your better judgement.
- If an adviser comes out to visit you, you might think of him as a 'guest' in your home and may not like to look rude by saying you're not interested.

Don't be afraid to say no if you're not interested ...

- If you meet your adviser at home, you may find it more difficult to cut short the meeting than if you had met at his offices, where you could leave whenever you wanted.
- Don't be afraid to tell your adviser if taking financial risk worries you. He may be able to put your mind at rest.
- A good adviser will be able to make investment recommendations covering the whole spectrum of risk.

*Chinchillas ...
tulip bulbs ...
gemstones ...*

- Ostriches, chinchillas, fine wine, tulip bulbs, classic cars, bloodstock, gemstones, doubloons, angora goats: these are not legally defined as investments. So there's no official compensation fund should the worst happen.
- If you are thinking of investing in a specialist market - a niche sector or an 'emerging' country - you should know something about that market.
- Don't invest in what you don't understand.
- Beware of investment 'fads'. The craze may move on, leaving you with investments no one wants to buy.
- No investment is so urgent that you have to hand over your money immediately.
- Take time to think about any investment proposals. Don't let yourself be pressured into making hasty decisions.
- If you know your investments involve evading tax which you should be paying, you can hardly complain if things go wrong.
- Not all business you do with a financial adviser may be covered by the investment watchdogs and the Investors Compensation Scheme.

*Please make your
cheque payable
to ...*

- Make sure you understand how the charges (fees or commission) work.
- Before you make your investments, check whether any penalties apply should you choose to cash them in early.
- Committing yourself at the outset into paying a set amount of money each month into a new policy can be a good savings discipline. But have you checked what happens if you can't afford the premiums one month?
- Ask about the tax implications of your investments. A qualified adviser should know and be able to advise you.
- Before you write out any cheques or hand over any money, check on the official Central Register (telephone: 0171 929 5652) whether your adviser is officially allowed to handle clients' money.

- If your adviser is not allowed to handle clients' money, make your cheque payable directly to the company where you're making the investment (eg the life insurance or unit trust company).
- If your adviser is officially allowed to handle clients' money, make sure any cheque you write is made payable to his authorised firm and not to any individual at the firm personally.
- Always make sure you get proper receipts on the firm's official headed notepaper, together with clear paperwork explaining the investments.

*A written
guarantee is only
as good as the
person providing
the guarantee ...*

- Remember always to read the small print before you sign anything.
- Check the paperwork, even if you know what you want and have explained this to your adviser. Misunderstandings and errors can still occur which could leave you with the wrong investment.
- 'Guaranteed' and 'assured' can sound very friendly words. But do you understand how the 'guarantee' or 'assurance' actually works?
- Remember that a 'guarantee' is only ever as good as the person providing the guarantee.
- Who is the 'guarantor' standing behind the guarantee? And what is his financial standing?
- If your adviser described the investments fairly, the paperwork should not contain any surprises - not even the small print.
- Don't be carried away by embossed certificates and gilded documents. What matters is what the paperwork is worth legally.
- Similarly, expect more than a scribbled note on the back of an envelope as proof of your investment.
- Be cautious of hand-written amendments and correction fluid on important documents.
- A certificate promising to buy something back from you at a fixed price is of little value if the company which issues the certificate goes out of business.
- If your adviser sends you paperwork from other businesses that he runs, make sure you are still dealing at all times with a firm that is fully authorised (Central Register telephone: 0171 929 3652).
- Check that letters you receive or agreements you sign are officially issued by the authorised company you thought you were dealing with. If not, find out why.

Keep your paperwork well organised ...

... it may not be you who has to sort it out

- You should be checking your financial statements as carefully as you should be checking your bank statements.
- If you are worried about the paperwork your adviser gives you, get in direct touch with the company where you are investing (eg the life insurance or unit trust company) to check everything is in order.
- Keep your paperwork safely, even if you think it is out of date and no longer important. If the worst did happen, you would need proof of your investments.
- It may be helpful for your close family to know about your financial arrangements, should anything happen to you.
- Keep all your paperwork well organised. It may not be you who has to sort out any problems.

Get promises and agreements confirmed in writing ...

- You want more than verbal assurances that your investments are 'doing well'. Ask for regular 'progress' reports in writing.
- Query changes to your portfolio and ask why the new investments are better.
- Get all advice in writing - *every time* your investments are changed.
- Don't rely on valuations given you just by your adviser. Find out if the value of your investments is quoted in a newspaper and check the price regularly yourself.
- Keep notes of all telephone conversations with your adviser: who you spoke to, the date and time you called and what was said.
- Ask your adviser to confirm in writing anything that was agreed or promised over the telephone or during meetings.
- Just because your shares fall in value doesn't automatically mean you've been given bad advice. Your adviser should have explained that investments can go down as well as up.
- If you're not happy, complain in writing to the firm.
- Don't be intimidated by jargon, especially if your instincts are telling you that this is an excuse and there is something going wrong.
- If you don't get a satisfactory answer from your adviser, report the matter to his or her watchdog.

Don't be intimidated by jargon ...
