

NATIONAL MARKET ADVISORY BOARD

REPORT TO THE CONGRESS

THE POSSIBLE NEED FOR MODIFICATIONS  
OF THE SCHEME OF SELF-REGULATION  
IN THE SECURITIES INDUSTRY  
SO AS TO ADAPT IT TO  
A NATIONAL MARKET SYSTEM

(Pursuant to Section 11 A(d)(3)(B) of the Securities Exchange Act of 1934)

December 31, 1976

NATIONAL MARKET ADVISORY BOARD

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December 31, 1976

President of the Senate  
Speaker of the House of Representatives  
Congress of the United States  
Washington, D. C.

Dear Sirs:

On behalf of the National Market Advisory Board, I am pleased to submit herewith the Board's Report to the Congress on the possible need for modifications of the scheme of self-regulation provided for in the Securities Exchange Act of 1934, as amended (the "Act"), so as to adapt it to a national market system. The Report is submitted pursuant to Section 11A(d)(3)(B) of the Act.

The subject of a national market system has been under, active discussion for approximately five years. The 1975 Amendments to the federal securities laws, which established the Board and called for the attached report, set forth the Congressional determination as to the goals of a national market system. With these goals in mind, and having consulted with a wide variety of persons interested or likely to participate in the establishment or operation of a national market system, the Board has begun to formulate its views as to the form such a system might take.

At the present time, the Board sees no need for the establishment of a new self-regulatory organization, nor for any other substantial modification of the scheme of self-regulation provided for in the Act.

The Board, however, does believe that the establishment of a national market system can best be facilitated, and that at least certain national market system facilities best administered, by one or more coordinating entities in which the self-regulatory organizations and the public are represented, but in which no one or two existing self-regulatory organizations have a dominant position. Such a coordinating agency could evolve from an industry-initiated effort currently in progress, but if one does not evolve from this or some similar effort, the Board may conclude that a new self-regulatory organization would be desirable.

Further, inasmuch as the Act has been recently amended to give the Commission the power to "authorize or require self-regulatory organizations to act jointly with respect to matters as to which they share authority ... in planning, developing, operating, or regulating the national market system ...," the Board at present sees no need for new legislation in order to implement the recommendations made in the Report.

The Board plans to consider further and set forth more fully its views on the form a national market system should take prior to the current expiration date of the terms of its members (September 30, 1977). By that time, a number of steps

towards the establishment of a national market system which have been undertaken or are about to be initiated will have been evaluated. If it then appears that it might be useful to update the recommendations contained in the accompanying Report, the Board will do so.

Respectfully submitted,  
John J. Scanlon  
Chairman

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## INTRODUCTION

1. Statutory Mandate

This Report is submitted to the Congress by the National Market Advisory Board (the “Board”) in accordance with Section 11A(d)(3)(B) of the Securities Exchange Act of 1934, as amended (the “Act”). [Footnote: Set forth in Appendix A is the full text of Section 11A(d) of the Act which directs the establishment of the Board and sets forth its responsibilities.]

The Board was established by the Securities and Exchange Commission (the “Commission”) in accordance with Section 11A(d)(1) of the Act on September 30, 1975. [Footnote: The Board was established as an advisory committee under the Federal Advisory Committee Act and it was on September 30, 1975 that its charter was filed as required by that act.] On that date the terms of the Board’s fifteen members began. [Footnote: John E. Leslie, Chairman of the Board, Bache Group, Inc., who was originally appointed as Chairman of the Board resigned from the Board on February 23, 1976. Upon his resignation, John J. Scanlon, retired Chief Financial Officer of American Telephone and Telegraph Company, who was one of the original members of the Board, was appointed Chairman. On April 28, 1976, Robert M. Fomon, Chief Executive Officer of E. F. Hutton & Company Inc., was appointed to fill the unexpired portion of Mr. Leslie’s term.] As required by the Act, these members come from various geographic areas of the United States, and a majority are associated with brokers and dealers. The persons not so associated are representative of the public and have a knowledge of the securities markets of the United States. Biographical information relating to each member is set forth in Appendix B.

The Act assigns to the Board three responsibilities. The first, in order of appearance in the statute, is to “formulate and furnish to the Commission its views on significant regulatory proposals made by the Commission or any self-regulatory organization concerning the establishment, operation, and regulation of the markets for securities in the United States.” [Footnote: Section 11A(d)(2) of the Act.] The second is to study and make recommendations to the Commission as to the steps it finds appropriate to facilitate the establishment of a national market system. [Footnote: Section 11A(d)(3)(A) of the Act.] The third is to submit this Report to the Congress on the possible need for modifications of the scheme of self-regulation in the securities industry as presently provided for in the Act so as to adapt it to a national market system.

The statute states that in carrying out its responsibilities “the Advisory Board shall consult with self-regulatory organizations, brokers, dealers, securities information processors, issuers, investors, representatives of Government agencies, and other persons interested or likely to participate in the establishment operation, or regulation of the national market system,” and the Board has consulted extensively with such persons, as detailed below. [Footnote: Section 11A(d)(3)(C) of the Act.]

## 2. Historical Context

The subject of a national market system has been under active discussion for approximately five years. [Footnote: The concept of a central, or national, market system was first mentioned officially in the Letter of Transmittal, Institutional Investor Study Report of the Commission, March 10, 1971. The first major discussion of the subject by a securities industry representative was in the Report to the Board of Governors of the New York Stock Exchange; The Securities Markets by William McChesney Martin, Jr., August 9, 1971. After extensive hearings held in October and November, 1971, the Commission issued its first statement devoted to the subject, the Statement on the Future Structure of the Securities Markets, February 2, 1972. The first major Congressional statements on the subject were in the reports on its Securities Industry Study issued by the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce in August 1972, and by the Subcommittee on Securities of the Senate Committee on Banking, Housing, and Urban Affairs in February 1973.]

During this period there has been a succession of advisory committees which have studied, stimulated public discussion of, and helped define the concept. Thus the Board had the benefit of the work of the three advisory committees established by the Commission in 1972, whose work was heavily relied upon by the Commission in formulating its 1973 Policy Statement on the Structure of a Central Market System, and of the work of the Advisory Committee on the Implementation of a Central Market System, better known as the "Yearley Committee" after its chairman, which was formed in 1974 and submitted its final report to the Commission in September 1975. However, this Board is the first advisory body concerned with the structure of the securities markets to act under Congressional direction and the first to have the benefit of Congressional determinations with respect to the goals of a national market system. [Footnote: These are contained in Section 11A(a)(1) of the Act, which was added to the law in 1975, and which is set forth in Appendix C.]

### 3. How the Board organized To Accomplish its Tasks

The Board has met regularly in public meetings for two days each month. Its first meeting was held in October 1975. The Board initially decided that in order to accomplish its three tasks it would be advisable for its members to review and study together the rather complex areas relating to a national market system with which the Board would have to deal, so that its members might have a common basis of understanding of the significant issues involved. Accordingly, the Board delineated seven subject areas which it believed would be relevant to its deliberations. They were: the composite limit order book; trading rules; administration, or governance, of a national market system; market making; the role of issuers; access to and membership in the system; and clearance and settlement.

These topic areas served both as a means of organizing the Board's initial, educational discussions and as a basis for working groups, composed of Board members, to study each topic in more depth and make a presentation to the full Board. Following each presentation, the Board discussed the subject based on the presentation and on materials prepared by the Board's staff. [Footnote: The Board chose its staff from among outside applicants and existing Commission employees to provide it full-time support in carrying out its responsibilities. Brief biographical information relating to each staff member is set forth in Appendix D.] This educational process, which occupied most of the first eight meetings, was substantially completed by the end of May 1976.

The Board also determined that it would need additional assistance in the technological area since it recognized that a national market system would utilize, to an as yet undetermined degree, data processing and communications technology. Accordingly, in May 1976 ten persons were asked to serve as voluntary Technical Consultants to the Board. Five of these are associated with the operations departments of broker-dealers, three with self-regulatory organizations, and two with independent consulting or service firms. All are knowledgeable in this field and have given generously of their time. [Footnote: The names and associations of the Technical Consultants are set forth in Appendix E.]

In accordance with the statutory direction to consult with persons interested or likely to participate in the establishment, operation, or regulation of the national market system, the Board, as one of its first acts, requested comments generally on such subjects. This request was published as a release by the Commission in November 1975 and a copy is attached hereto as Appendix F. In addition, the Board wrote specifically to a number of persons who it thought might be interested in commenting and requested them to do so.

The Board received some fifty submissions, ranging from short statements on specific issues to complete proposals for a national market system. The name of each person who has made a written submission to the Board is set forth in Appendix C. The Board felt that it would be helpful to meet with representatives of certain of the commentators in order to discuss in more detail their individual submissions and questions raised thereby. The study of submissions proceeded concomitantly with the Board's review and study of issues and was substantially completed by August 1976.

#### 4. Nature of Scheme of Regulation Dependent on Form National Market System to Take

One fact which became clear to the Board during this educational and consultative process was that it could not intelligently make recommendations

with respect to the possible need for modifications of the scheme of self-regulation in the securities industry so as to adapt it to a national market system except in relation to its developing conceptions of the form the national market system was to take.

Board members have begun to develop views on the form that a national market system might take, in part as a result of the aforementioned educational and consultative process. These views have also developed in the process of the Board's fulfilling its statutory responsibility to comment on significant regulatory proposals relating to a national market system. In this regard, the Commission has asked the Board to respond to it on a number of regulatory proposals by certain specified dates, and complying with these requests has required the Board to begin to articulate its views with respect to the emerging national market system. [Footnote: For example, in February 1976, the Commission asked for the Board's views on issues which might be relevant to the establishment of a composite limit order book. The Board's response was incorporated in the Commission's request for comments on such issues. [Securities Exchange Act Release No. 12159 (March 2, 1976)]. In September 1976, the Board responded to the Commission's request for the Board's views with respect to the elimination of exchange rules prohibiting in-house agency cross transactions in listed securities by members. [The request was contained in Securities Exchange Act Release No. 11942 (December 19, 1975), page 40]. The Board is currently in the process of forwarding its views to the Commission with respect to the Commission's proposals regarding the establishment of a composite limit order book. The Board is also in the process of preparing its response to the Commission's request for its views as to whether member firms ought to be permitted to engage off exchange floors in transactions in listed securities as principals. [The request was contained in Securities Exchange Act Release No. 11942 (December 19, 1975), page 28].]

##### 5. Establishment of National Market System Involves a Series of Steps - Implications of Such Conclusion

A second fact which became clear to the Board early in its deliberations was that the establishment of a national market system is a process which involves a series of steps. In fact, this seems to be implied by the Act itself, which calls upon the Board to make recommendations "as to the steps it finds appropriate to facilitate the establishment of a national market system." [Footnote: Section 11A(d)(3) of the Act, emphasis added.] Because it is difficult to predict with certainty the consequences of taking any particular step, and since the effects of an earlier action are likely to impact on the desirability of taking a planned later action, the further in the future one attempts to plan, the more difficult it is to be precise about the steps it will be appropriate to take at the future time. Therefore, in making recommendations at this time as to the need for modifications of the scheme of self-regulation so as to adapt it to a national market system, the Board

can speak with some confidence only with respect to the near future. However, the Board will continue to exist at least until September 30, 1977 (the current expiration date of the appointments of each of its members). By that time the longer range implications of a number of important steps recently taken or soon to be taken (discussed below) may become more clear. Conclusions reached by Board members with respect to such implications may result in the Board having further views as to the need for modifications of the scheme of self-regulation.

For this reason, and because by September 30, 1977, the Board will also have set forth further views with respect to the form it believes a national market system should take (which as noted above also may affect its views as to the need for modifications of the self-regulatory scheme) the Board plans to report to the Congress again in September 1977 on the subject of this Report if it appears at that time that it might be useful to update the recommendations made herein.

## **RECOMMENDATIONS**

### **1. No Need At This Time for a National Market Regulatory Board**

The Act specifically requires that the Board study and report to the Congress on the need for the establishment of a new self-regulatory organization (referred to in the Act and hereinafter as a "National Market Regulatory Board" or "Regulatory Board") to administer the national market system. [Footnote: Section 11A(d)(3)(B).] Based on its deliberations to date, the Board sees no present need for a Regulatory Board. Because at this time the exact form which the national market system may take is not clear, the Board cannot now advise as to whether, at some later stage in the development of a national market system, it would be desirable for a Regulatory Board to be created.

However, the Board believes that the establishment of a national market system can best be facilitated, and that at least certain national market system facilities best administered, by one or more coordinating entities in which the self-regulatory organizations and the public are represented, but in which no one or two existing self-regulatory organizations have a dominant position. There recently has been formed an industry organization, which is discussed below in connection with the systemwide protection of limit orders. This organization might serve as a nucleus from which such a coordinating entity could evolve. If it or some similar effort does not so evolve, the Board may conclude that some form of Regulatory Board is desirable.

As suggested above, if by September 30, 1977 the Board has further recommendations to make with respect to the possible establishment of a Regulatory Board in the national market system, it will make a further report to the Congress with respect thereto.

## 2. No Need at this Time for Legislation Regarding Scheme of Self-Regulation

The Act states that this Report shall include such recommendations for new legislation as the Board deems appropriate. [Footnote: Section 11A(d)(3)(B).] Because the Board at this time is not recommending any substantial modifications of the scheme of self-regulation provided for in the Act, and inasmuch as the Act has been recently amended to give the Commission the power to “authorize or require self-regulatory organizations to act jointly with respect to matters as to which they share authority in planning, developing, operating, or regulating the national market system . . .”, the Board at this time sees no need for new legislation in order to implement the recommendations made herein with respect to the administration of a national market system. [Footnote: Section 11A(a)(3)(B).]

## **DISCUSSION AND ANALYSIS**

### 1. Steps Recently Taken or About to be Taken Towards the Establishment of a National Market System and Their Relation to the Scheme of Self-Regulation

During the last year and a half a number of important steps have been taken towards the establishment of a national market system. Generally, these can be divided into three categories: those relating to the establishment of facilities which would have the effect of linking markets; those relating to the strengthening of competition among various elements of the industry; and those directed at increasing the efficiency with which transactions are handled. Reviewing each of the steps which have been, or are about to be, taken from the viewpoint of their implications for the scheme of self-regulation should help to make clear why the Board has concluded that there is no need at this time for a Regulatory Board or for legislation affecting the self-regulatory scheme.

#### A. Component Facilities - Linking of Markets

One of the most specific statements of Congress with respect to the establishment of a national market system is its finding that “the linking of all markets for qualified securities through communication and data processing facilities will foster efficiency, enhance competition, increase the information available to brokers, dealers, and investors, facilitate the offsetting of investors’ orders, and contribute to best execution of such orders.” [Footnote: Section 11A(a)(1)(D) of the Act.]

Thus it is not surprising that several major facilities linking markets have been, or are in the process of being, developed.

(1) Consolidated last sale reporting facility.

On June 16, 1975, there became fully operational a facility for reporting all transactions with respect to New York Stock Exchange listed issues occurring on all exchanges and in the over-the-counter markets. [Footnote: Transactions not involving a broker-dealer are not presently required to be reported.] Each report shows the stock symbol, size, and price of the transaction and identifies the market in which it took place. On March 1, 1976, a similar facility became fully operational with respect to stocks listed on the American Stock Exchange and selected issues listed on other exchanges. These facilities are referred to as the consolidated tape. [Footnote: Actually, the information which is made available can be displayed in various formats other than on a moving tape. For example, services are now available which enable a broker, dealer or investor to recall on a cathode ray tube screen information regarding the most recent last sale, in any market, for a particular stock included in the consolidated tape. The use of a "high speed line" provides the ability to display on a cathode ray tube screen current information on the stream of transactions with respect to any designated tape security regardless of any delays in the moving tape during periods of heavy trading.] (The first system is known as "Network A" and the second as "Network B".)

Securities Exchange Act Rule 17a-15 proposed in March 1972 and adopted in November 1972 mandated the development of the consolidated tape. The rule was proposed by the Commission after it became clear that an industry effort would fail to agree on how to develop such a tape. That industry effort, begun in the fall of 1971, involved a working committee consisting of representatives of the New York, American, Midwest, Pacific and Philadelphia Stock Exchanges and the National Association of Securities Dealers, Inc. ("NASD"). [Footnote: Then, the PBW Stock Exchange.] A basic disagreement arose. The New York Stock Exchange took the position that as an interim step markets other than the New York and American Stock Exchanges should disclose transactions in their markets separately from those two Exchanges, and that a full consolidated tape be developed only after a national market system was in place. The other exchanges and the NASD took the position that a true consolidated tape should be implemented immediately as a first step toward a national market system.

Rule 17a-15 required the filing of a plan providing for the dissemination of last sale data on a consolidated basis. Self-regulatory organizations would be prohibited from releasing last sale data on a current basis without a plan declared effective by the Commission. In March 1973, the New York, American, Midwest, Pacific and Philadelphia Stock Exchanges and the NASD filed a joint plan pursuant to Rule 17a-15 with the Commission. In May 1974, after public comment, including comment by plan participants, and several amendments to the plan, the Commission approved the plan, as amended.

In conjunction with the development of the plan an organization was created to administer the plan. This organization is the Consolidated Tape Association (“CTA”). The CTA consists of eight voting members. The New York and American Stock Exchanges each have two votes and the Midwest, Pacific, and Philadelphia Stock Exchanges and the NASD each have one vote. Five affirmative votes are necessary for CTA action. All amendments to the plan, with two minor exceptions, are subject to the veto of either the New York or American Stock Exchange. [Footnote: For example, the Securities Industry Automation Corporation (“SIAC”), a jointly owned subsidiary of the New York and American Stock Exchanges, was appointed the processor of the consolidated tape for a five year term and any replacement of SIAC during such period requires an amendment to the plan. The appropriateness of the appointment of SIAC as the processor was the subject of disagreement. Some believed that the processor should be chosen as a result of competitive bidding. The New York and American Stock Exchanges were of the view that the processor of the then existing tape (which contained the bulk of the transaction reports to be included in the consolidated tape) should be continued as the processor of the consolidated tape.]

The CTA also has non-voting members who, prior to the start-up of the consolidated tape, signed the plan and who send last sale reports to SIAC for retransmission on the consolidated tape. These non-voting members are the Boston and Cincinnati Stock Exchanges and Institutional Networks Corporation (operators of the “INSTINET” service). [Footnote: Prior to withdrawing its registration as a national securities exchange, the Detroit Stock Exchange was also a non-voting member.]

The development of the tape plan and the tape system itself were delayed by many disputes over what in the opinion of some were regulatory issues and in the opinion of others economic issues. The disputes involved such matters as trading hours, criteria for eligible securities, sharing of costs and revenues connected with the consolidated tape, trading halt procedures, appropriate equal regulation among markets and the appropriate last sale reference point for short selling rules. Also, because the tape plan was drafted to make the NASD’s rules regarding the collection of third market transactions an amendment to the plan, and thus subject to a New York Stock Exchange veto, the rules on how third market trades are collected and reported became a point of contention rather than an internal matter for the NASD. Most of these issues ultimately required Commission involvement for their resolution. While there were technical delays, which are often inevitable in projects of this scope and type, they were not the primary source for the overall delay in the creation of the consolidated tape.

The consolidated tape is now in successful operation. [Footnote: This is not meant to imply any opinion as to whether or how the consolidated tape will or should evolve in the future.] Experience with its development and administration

has provided several important insights regarding the relationship of the existing scheme of self-regulation and the establishment and administration of national market system facilities.

The consolidated tape experience highlights the fact that the self-regulatory organizations are required by their circumstances to play two entirely different roles. On one hand, they are required to be quasi-governmental bodies, concerned with implementing the spirit and letter of the securities laws. On the other hand, they represent the economic interests of particular market places and must be concerned with preserving and enhancing the position of such market places. The first of these roles makes them, given their intimate relationship with industry members, attractive candidates for coordinating the establishment of a national market system facility. The latter of these roles insures that cooperation among them will be difficult.

Experience with the consolidated tape showed that for such a cooperative effort to be successful the Commission may have to become actively involved in the effort as the situation requires. Although some of the participants in the tape project from time to time questioned the Commission's authority, the Commission persevered and the project was brought to a successful conclusion. The 1975 amendments to the securities laws have given the Commission more explicit and more extensive powers than it previously had in this regard. Thus, the Commission now has even a greater ability to foster cooperation among the self-regulatory organizations, if that course of action appears desirable to it.

More specifically, the CTA experience suggests the inadvisability of including in the charter of a national market system coordinating or governing entity any veto, or other measure, which would give one or two of the participating self-regulatory organizations the ability to dominate such entity.

## (2) Composite quotation system

Currently there are available from two private services composite bid and asked quotations emanating from participating exchanges relating to securities listed on the New York Stock Exchange which are also traded on other exchanges.

[Footnote: Since September 1975, GTE Information Systems, Inc. has provided a service which displays only the best bid and offer, which are updated automatically, from among various exchanges (but not the third market).

Institutional Networks Corporation recently began offering a service which presents a simultaneous display (montage) of quotations from each exchange rather than displaying only the best bid and offer from among all the exchanges.]

It is expected that a third service relating to New York Stock Exchange listed securities but including quotations from non-exchange ("third market") market makers will become available soon. [Footnote: The NASD has announced plans to make such a composite quotation service operational in January 1977. It too

will be capable of displaying a montage of quotations from several market centers at the same time.]

The existing services were developed through private initiative but reflect the end-product of a number of experimental regulatory approaches taken by the Commission. In March 1972, the Commission proposed a brief rule, Rule 17a-14, which would have simply directed the self-regulatory organizations to make quotation information available to vendors. [Footnote: Securities Exchange Act Rule 17a-14, as proposed in Securities Exchange Act Release No. 9529 (March 8, 1972)] In light of its experience with Rule 17a-15, however, which required the self-regulatory organizations to file plans for reporting information on completed transactions, the Commission, in August 1974, revised proposed Rule 17a-14 to require the filing of plans for reporting information with respect to quotations. [Footnote: Securities Exchange Act Rule 17a-14, as proposed in Securities Exchange Act Release No. 10969 (August 14, 1974).] As revised, the proposed Rule would have directed that such plans include certain requirements as to the conditions and manner in which quotations would be reported. The Commission eventually determined, however, to take an approach even less structured than the original version of the proposed rule. In March 1975, instead of adopting proposed Rule 17a-14, the Commission by letter formally requested all national securities exchanges to eliminate restrictions on access to or use of quotation information disseminated by such exchanges to any vendor. [Footnote: Securities Exchange Act Release No. 11288 (March 11, 1975).] It was hoped that this approach would give freer play to competitive forces among market centers, and would lead to the eventual development of a composite quotation system through private initiative.

In keeping with the Commission's request, the self-regulatory organizations made their quotation information available to vendors without restrictions, but few persons subsequently subscribed to the services offered. The vendors urged that the lack of interest resulted at least in part from inadequacies in the "quality" of the quotation information available to them. The Commission has recently proposed a rule to require all self-regulatory organizations to make available to vendors quotation information that would be more useful to brokers, dealers and investors than that currently available. [Footnote: Proposed Rule 11Ac1-1, Securities Exchange Act Release No. 12570 (July 29, 1976). First, timely updating of quotations would be required. Second, the self-regulatory organizations would have to make available the size of the quotation, that is the amount bid or offered, if specified by the specialist or market maker. In addition, quotations emanating from a market center would have to be "firm" up to the size quoted (or if size is not specified, for a normal unit of trading). This means that a specialist or third market maker must stand ready to execute a transaction in any amount up to the amount of his published quotation at the quoted price. Exceptions to the firmness requirement are included to provide (i) for an intervening transaction in the security appearing on the consolidated tape, or occurring in his market place and not yet reported on the tape. by allowing

persons a short period to change their quotation, and (ii) for an updated quotation which has been transmitted but not yet displayed.]

Efforts with respect to the development of a composite quotation system may show whether it is possible for a national market system facility to be developed through the interplay of competitive forces, with Commission assistance when necessary, but without the creation of a new self-regulatory or coordinating body. This approach with respect to the development of a useful composite quotation system seems to be promising, but more time will be needed before a firm judgment can be made with respect to the success of these steps.

(3) Systemwide protection of limit orders. [Footnote: A simple limit order is an order to buy or sell a specified quantity of a security at a stated price or better. The order may be good for a specified period of time or good until cancelled. Limit orders constitute a significant portion of the orders placed with respect to listed securities.]

From the early stages of discussions about a national market system, various persons have suggested that a computerized central limit order repository (a composite book) or some similar facility might be an important part of such a system. [Footnote: See, for example, Commissioner Phillip A. Loomis's statement on November 8, 1971, during the Commission hearings In the Matter of the Structure, Operation, and Regulation of the Securities Markets, at page 2329, and the statement of A. C. Becker & Co. Incorporated presented at such hearings on November 16, 1971, at page 12.] During the last five years the concept of a composite book has been discussed in many contexts and the concept has been significantly refined. [Footnote: See, for example, Securities Industry Study Report of the Subcommittee on Securities, Committee on Banking, Housing, and Urban Affairs, United States Senate, February 1973. at page 112, and Reports of the Advisory Committee on the Implementation of a Central Market System, dated September 12, 1975, pages 15, 78-83.]

As noted above, the Board, early in its deliberations, singled out the composite book as one of the seven subjects it would study in assessing how a national market system ought to be established. Recently, impetus for the Commission taking action with respect to a composite book arose from discussions concerning the removal of restrictions on off-board trading by members of national securities exchanges. [Footnote: Securities Exchange Act Release No. 11942 (December 19, 1975), pages 47-53.] Most recently the Commission observed that a composite book would not only provide protection for public limit orders if prohibitions on off-board trading were removed, but its establishment would also enhance competition among market makers (both exchange and third market), link markets through communications and data processing equipment, and provide for the more efficient handling of limit orders. [Footnote: Securities Exchange Act Release No. 12159 (March 2, 1976), p. 2.] However, in the same

release the Commission stated that it was interested in the comments of interested parties as to alternatives to a composite book system.

Although some have expressed concern that a composite limit order book would cause specialists to reduce their market making activity, as well as threaten the viability of exchange floors as trading arenas, the Board, in its report to the Commission on the composite book, is stating that it believes that the development of facilities which would provide protection of limit orders to the maximum extent practical is an important objective of a national market system. [Footnote: The Board decided to use the phrase "protection of limit orders to the maximum extent practical" after considering various other formulations including "full protection." The Board felt the latter would mandate the establishment of a composite limit order book, but that, in light of practical considerations, it should remain open for the industry and the Commission to consider alternatives that would achieve maximum practical protection but fall short of achieving full protection. Several members of the Board felt that available data indicate the technological and economic practicality of a composite limit order book as described below and, unless future evidence is to the contrary, that nothing short of such a composite limit order book should be accepted as protecting limit orders in a national market system to the maximum extent practical.] The Board's recommendations are based on an analysis which concluded that limit orders not only serve a useful purpose for investors but also contribute to the strength and orderliness of the market.

The Board is also advising the Commission that it strongly supports the idea that the industry be allowed the primary role in any effort to achieve this objective as opposed to its being achieved by action mandated by the Commission. The Board, in its public deliberations, which included oral and written presentations by several industry groups, discovered a wide range of industry feeling, from strong support to outright opposition, to a composite book. It is also aware of an organization, initiated by the Securities Industry Association, of representatives of seven stock exchanges and the NASD (the National Market Association ("NMA")) which was formed to "analyze alternative methods for enhancing limit order protection, increasing competition between and among market places for listed securities, and increasing communications between and among such marketplaces ..." [Footnote: Quotation from press release issued on September 27, 1976. On that date representatives of the American, Boston, Midwest, New York, Pacific and Philadelphia Stock Exchanges and the NASD, formed the National Market Association. Subsequently, the Cincinnati Stock Exchange joined the association.]

The Board is aware of several proposals either presented to it or discussed by industry entities which, according to the various proponents, could provide an acceptable degree of protection of limit orders and increased competition among specialists and market makers. The Board judged that the NMA within six months from its inception in September 1976, should be able to analyze alternatives to a

composite book and agree upon a course of action. In light of the significant industry interest in attempting to develop on its own a system of enhanced limit order protection, the Board voted to encourage the industry effort and to make its decision known to the Commission. It is the feeling of the Board that if the newly formed NMA can develop a suitable alternative to a composite book by March 31, 1977, then the Commission should consider it favorably.

Since it is not clear that a suitable alternative can be found and agreed upon within such period and because, in the Board's view, a composite book, or some facility, arrangement, or business practice which would achieve substantially the same ends, is an important element of a national market system with respect to which action should be taken in the near future, the Board is recommending that the Commission pursue its analysis and decision-making process with respect to a composite book while the industry efforts are proceeding. To assist the Commission in this effort pursuant to the responsibilities of the Board under the Act and in response to the request of the Commission, the Board is submitting to the Commission its views with respect to various characteristics of a composite book and means of facilitating its development.

The Board is recommending that if it becomes necessary for the Commission to direct the implementation of a composite book, then the Commission should request the submission of plans to establish a composite book with characteristics which the Commission should specify in its request. The Board is recommending that the Commission in any such request specify that plans submitted should include provision for a body which would administer the establishment and operation of the book. The Commission should state that such body might be in the form of a coordinating vehicle for the self-regulatory organizations with no one or two having a dominant position in the body. The Commission should also state that it appears appropriate for such a body to include some representation of the public. In addition, the Commission ought to require that any plans submitted clearly set forth the authority of the body and its decision-making process.

If a suitable alternative to a composite book should be developed it is likely that some new body would be required in order to establish and administer any new facilities which were part of the proposal. [Footnote: For example, it would appear that some entity would have to be given authority to choose among, and contract with, persons desiring to supply equipment for the new facility. Such an entity would also seem to be needed to establish rules applicable to users of the facility with respect to the use thereof.] The Board believes that any such body should have the same characteristics which the Board recommends the Commission require in entities proposed to administer a composite book system. It is likely that such an entity could be created without the need for legislation. On the other hand, it may be determined that the kind of authority which such an entity ought to have, or the positions taken by the self-regulatory organizations with respect

thereto, necessitates legislation in order to establish an entity with the requisite power.

As stated above, should this happen during the life of the Board, it will so report to Congress.

(4) Possible intermarket execution system.

The NMA has tentatively proposed the establishment of an intermarket execution system which would enable a buyer in one marketplace to meet a seller in another through facilities linking all participating marketplaces. Each participating market place would be required to provide a connection to the central system to each of the specialists or market makers in its marketplace. A number of open questions exist and the NMA has established two committees to deal with these. At this time it is difficult to determine how the establishment of an intermarket execution system would affect the scheme of self-regulation, and even whether a new entity would be required in order to administer it.

B. Strengthening of Competition

Within the last year and a half, a number of actions have been taken to strengthen competition among brokers and dealers. For example, on May 1, 1975, Securities Exchange Act Rule 19b-3 became effective, except with respect to certain floor brokerage. It prohibited national securities exchanges from having rules which require their members to charge any person a fixed rate of commission for transactions on or involving the facilities of the exchange. As a result commission rates, measured in cents per share and as a percent of the principal amount of the order, have declined significantly (35% and 30%) for institutional customers and fractionally (2% and 6%) for individual customers (rates on the smallest individual orders, however, increased by 2% on both bases). [Footnote: U.S. Securities and Exchange Commission, Third Report to Congress on the Effect of the Absence of Fixed Rates of Commissions, August 10, 1976, Exhibits 3, 4 and 5 at pages 12,14 and 15.] On May 1, 1976 the prohibition on fixed rates became effective with respect to exchange floor brokerage (intra-member) rates as well. During 1976, the New York Stock Exchange began to permit competing specialists on its floor, and the Commission informed the New York Stock Exchange that the Securities Acts Amendments of 1975 did not permit the exchange to limit its membership based on the nationality of the firm involved or of its parent. The effects of these actions are just beginning to be felt by the industry.

In addition, during the last year a number of other steps have been taken to strengthen competition among markets. For example, on March 31, 1976, Securities Exchange Act Rule 19c-1 became effective, requiring that national

securities exchanges permit their members to take agency orders for listed securities to qualified third market makers and non-member block positioners after satisfying orders in the limit order book. (Prior to the adoption of the rule certain national securities exchanges, including the New York Stock Exchange, had rules which with minor exceptions required members to take all of their orders to an exchange floor.) Rule 19c-1 also provides that after January 2, 1977 members shall be permitted to bring such agency orders to qualified third market makers and non-member block positioners without having to clear the limit order book on the exchange. In August and October 1976, respectively, the American Stock Exchange and the New York Stock Exchange abolished their rules prohibiting the trading of the securities of an issuer on one such exchange if they were being traded on the other.

Currently, several more steps are being considered in order to strengthen competition among broker-dealers and among markets. For example, the moves to create more useful composite quotation systems, as discussed above, are expected to enhance competition among broker-dealers and among market makers and specialists. As noted above the NMA has tentatively proposed the establishment of an intermarket execution system which, if established, would be likely to increase competition among participating specialists and market makers. The Cincinnati Stock Exchange commenced operation in October 1976, and Institutional Networks Corporation has ready for operation, systems which are designed to increase competition among market makers and specialists.

[Footnote: The Cincinnati Stock Exchange System is WHAM ("Weeden Holding Corporation Automated Market"). It is a computer system into which dealers may enter firm bids and offers, with size, through remote terminals. Bids (or offers) at the same price are consolidated on an anonymous basis and displayed to the user as total shares bid for (or offered) at a given price. Brokers may view these markets through a broker terminal and execute against the market by entering a bid at the same price as a shown offer or by offering shares at the same price as a shown bid. If the bid/ offer is not acceptable, the broker may enter the customer's own bid or offer into the system thereby becoming part of the anonymous consolidated market offered to all users of the system. Institutional Networks Corporation has proposed a system called UNIMART, which is based on subsystems already in use as part of the firm's INSTINET service. As described by the vendors, it can execute orders, either through automatic matching of orders, or as the result of negotiations conducted through the terminal. Participants who have entered "indications of interest" can be contacted, anonymously, through the UNIMART terminal, facilitating negotiated transactions of size. UNIMART also displays -- and dynamically updates -- all available quotations, on a montage basis. It also displays last sale information from the consolidated tape.]

However, the extent to which such systems will be used is as of yet unclear. In addition, the Commission has stated that by March 1, 1977 it will reconsider the appropriateness of restrictions which some national securities exchanges impose

on their members conducting principal transactions off the floor of the exchange. The resolution of this issue is likely to have an important effect on competition.

The Commission has a strong mandate to foster competition in the industry and considerable authority in order to carry out that mandate. There seems little which a new self-regulatory organization could add to this effort to strengthen competition. However, these steps to strengthen competition are likely to have a significant impact on the structure of the securities industry and the eventual form of the national market system, and thus they have implications for the scheme of self-regulation. As the nature of the consequences of these steps becomes more clear, the Board will be able to determine whether, and the extent to which, they make advisable significant changes in the self-regulatory scheme.

### C. Increasing Efficiency of Transaction Processing

Also within the recent past, a number of steps have been taken which have increased or should increase the efficiency with which transactions are processed. This is the intent of the proposed merger of the three largest clearing entities which the Commission has recently announced that it intends to approve, subject to certain conditions. [Footnote: Securities Exchange Act Release No. 12954 (November 3, 1976).] A number of the exchanges have adopted automated order handling procedures of various kinds which have had a similar effect. [Footnote: The Pacific Stock Exchange established COMEX ("Communications and Execution") in 1969 as a means for the automatic execution of odd-lot orders in dually listed issues. In 1973 the system was expanded to accommodate market and limit orders of 100 to 199 shares and in March 1976, to orders of up to 300 shares. Market and limit orders may be entered by brokers directly into the Pacific Stock Exchange computer facility through a common message switch and are executed automatically by formula, based on primary market transactions reported on the consolidated tape. The specialist generally takes one side of the transaction for his own account. DOT ("Designated Order Turnaround System") was inaugurated on a pilot basis by the New York Stock Exchange on March 1, 1976. Limited originally to market orders of 100 shares and a restricted number of firms, the service has been expanded to all brokers who have the capability of interfacing with the exchange's message switching facility and will handle orders of 100 to 199 shares. The DOT system provides for the routing of market orders to a terminal printer at the specialist's post rather than to the broker's Own floor booth. Execution of market orders is handled by the specialist representing the order in the "crowd" in place of the broker's own floor representative and executions are reported back to the entering broker via an input terminal at the specialist's post. Limit orders may also be transmitted to the specialist via the DOT facilities and some brokers have their own communications systems programmed to recognize and route appropriate market and limit orders via DOT without manual intervention The WHAM service offered by the Cincinnati Stock Exchange is described above.]

It appears that a new self-regulatory organization would add little to the movement to increase the efficiency with which transactions are processed. The Commission has significant power to achieve this end. It also appears that the forces of competition will tend to give rise to innovations which will further this purpose.

## 2. Coordination Among Self-Regulatory Organizations

There have been suggested two different ways that a new self-regulatory body might be of use. One is as a means of eliminating the overlapping authority and duplication of efforts devoted to the regulation of members by the existing self-regulatory organizations. The other is as an entity to implement and administer new and possibly existing national market system facilities. The Board has concluded that at least for the present the needs in both of these areas would best be served, not by the creation of a new self-regulatory body, but by better coordination among existing self-regulatory organizations. Such increased coordination would also serve a third end, facilitating the participation of the self-regulatory organizations in the establishment of a National Market System.

### A. Overlapping Authority and Duplication of Regulatory Efforts

Section 17(d)(1) of the Act gives the Commission extensive power to reduce overlapping authority and duplication of efforts. [Footnote: The full text of Section 17(d)(1) is set forth in Appendix H.] Pursuant to this section the Commission has adopted a rule which it believes will lead to the substantial reduction of duplication by encouraging existing self-regulatory organizations to work together to achieve such end. [Footnote: Rule 17d-2 [Securities Exchange Act Release No. 12935 (October 28, 1976)]. It provides that any two or more self-regulatory organizations may, by March 15, 1977, file with the Commission a plan for allocating among themselves a variety of specified regulatory functions affecting their members. Earlier, in Rule 17d-1, [Securities Exchange Act Release No. 12352 (April 20, 1976)] the Commission undertook to designate for each broker-dealer which is a member of more than one self-regulatory organization, one organization which would have the responsibility for inspecting that broker-dealer for compliance with applicable financial responsibility rules.] Public hearings were held with respect to the rule in December 1976 in order to stimulate discussion and cooperation in this area. The self-regulatory organizations have been consulting among themselves and considering a variety of proposals. [Footnote: The NASD has recommended the creation of a "consolidated industry compliance entity" that would have full rule-making authority, subject to Commission approval, and regulate all broker-dealers. It would not participate in the governance of any exchange or any national trading facility. In addition, it would not have any rulemaking authority or enforcement responsibility with

respect to the operation of the trading facilities of the various marketplaces, or have any control over such things as access to the facilities of these marketplaces or the establishment and enforcement of listing standards. The New York Stock Exchange has suggested the possibility of creating a new industry organization that could provide a broad spectrum of audit and examination services, by contract, to present self-regulators.] While it is too early to reach a definitive conclusion, in light of the foregoing it appears to the Board that it is not necessary at this time to modify substantially the scheme of self-regulation in order to substantially reduce the overlapping jurisdictions and duplication of effort of self-regulatory organizations in supervising their members.

#### B. Establishing and Administering New National Market System Facilities

As noted in connection with the discussion relating to the establishment of facilities to give systemwide protection to limit orders, a new coordinating vehicle is likely, to be required to implement and administer the system. At the Board's December meeting, the NMA appeared and described its progress to date as well as the prospects for further cooperative efforts towards development of an alternative to a composite book. The Board was impressed by the NMA's progress to date and by the expressions of unanimity among the NMA members of their determination to settle further specific questions in the near future. The Board expects to hear further from the NMA as they resolve outstanding questions and to comment to them and to the Commission on their progress. Nevertheless, because the existing self-regulatory organizations represent the competing economic interests of particular market places, difficulties may arise in the process of their attempting to create a new coordinating vehicle to establish and administer new facilities. As suggested by the consolidated tape experience, the chances of their joint effort being successful may be improved significantly if the Commission takes an active role in the process. Thus, it is possible that the new NMA may give rise to the new coordinating entity, or the Commission may have to use its authority to require joint action in order for an effective body to be created. It is also possible that because of the kind of authority which such an entity ought to have, or the positions taken by the self-regulatory organizations with respect thereto, new legislation will be required to establish such an entity. Events during the next several months should help clarify what, if any, kind of governmental action will be needed.

#### C. Facilitating Participation in the Process of Establishing a National Market System

Finally, there is a third, more general, area in which coordination among the self-regulatory organizations might prove useful; that is in facilitating their participation in the process of establishing a national market system.

Although it may often be difficult for the self-regulatory organizations, because of their divergent economic interests, to agree with respect to the taking of particular steps toward the establishment of a national market system; nevertheless, encouraging interaction among them, including face-to-face discussions among their representatives at various levels on subjects relevant to the establishment of a national market system, may be helpful in a variety of ways. It could help clarify the issues, elucidate potential effects of specific steps being contemplated, and suggest grounds for suitable compromises.

To some extent, this Board has served some of these purposes. It is possible that the NMA may also serve these ends. The entity created to establish and administer facilities for the systemwide protection of limit orders might also be an appropriate vehicle. Thus, depending on developments, it may be advisable for the Commission to extend appointments to the Board beyond September 30, 1977. If during 1977 this should appear desirable, the Board will so advise the Commission.

## **CONCLUSION**

Within the last two years a number of steps have been taken towards the establishment of a national market system. The Board, with such steps in mind, is currently in the process of formulating its views on the form a national market system should take. The Board believes that the creation of one or more coordinating entities in which the self-regulatory organizations and the public are represented, but in which no one or two organizations have a dominant position, would facilitate the establishment of a national market system and is needed to administer at least certain national market system facilities. While events may suggest that legislation is needed to create such an entity, at the present time the Board sees no need for legislation creating a new self-regulatory organization or otherwise affecting the scheme of self-regulation.

Should the Board's views as to the need for modifications of the scheme of self-regulation in the securities industry so as to adapt it to a national market system change or require updating in light of its further deliberations or events occurring prior to the expiration of the current ten of its members (September 30, 1977), the Board will so report to the Congress.

## **APPENDICES**

### **APPENDIX A**

**Section 11A(d) of the Securities Exchange Act of 1934**

11A(d)(1) Not later than one hundred eighty days after the date of enactment of the Securities Acts Amendments of 1975, the Commission shall establish a National Market Advisory Board (hereinafter in this section referred to as the "Advisory Board") to be composed of fifteen members, not all of whom shall be from the same geographical area of the United States, appointed by the Commission for a term specified by the Commission of not less than two years or more than five years. The Advisory Board shall consist of persons associated with brokers and dealers (who shall be a majority) and persons not so associated who are representative of the public and, to the extent feasible, have knowledge of the securities markets of the United States.

(2) It shall be the responsibility of the Advisory Board to formulate and furnish to the Commission its views on significant regulatory proposals made by the Commission or any self-regulatory body concerning the establishment, operation, and regulation of the markets for securities in the United States.

(3)(A) The Advisory Board shall study and make recommendations to the Commission as to the steps it finds appropriate to facilitate the establishment of a national market system. In so doing, the Advisory Board shall assume the responsibilities of any advisory committee appointed to advise the Commission with respect to the national market system which is in existence at the time of the establishment of the Advisory Board.

(B) The Advisory Board shall study the possible need for modifications of the scheme of self-regulation provided for in this title so as to adapt it to a national market system, including the need for the establishment of a new self-regulatory organization (hereinafter in this section referred to as a "National Market Regulatory Board" or "Regulatory Board") to administer the national market system. In the event the Advisory Board determines a National Market Regulatory Board should be established, it shall make recommendations as to:

- (i) the point in time at which a Regulatory Board should be established;
- (ii) the composition of a Regulatory Board;
- (iii) the scope of the authority of a Regulatory Board;
- (iv) the relationship of a Regulatory Board to the Commission and to existing self-regulatory organizations; and
- (v) the manner in which a Regulatory Board should be funded. The Advisory Board shall report to the Congress, on or before December 31, 1976, the results of such study and its recommendations, including such recommendations for legislation as it deems appropriate.

(C) In carrying out its responsibilities under this paragraph, the Advisory Board shall consult with self-regulatory organizations, brokers, dealers, securities information processors, issuers, investors, representatives of Government agencies, and other persons interested or likely to participate in the establishment, operation, or regulation of the national market system.

## APPENDIX B

### National Market Advisory Board Members

Milton H. Cohen is a partner of the firm of Schiff, Hardin & Waite, Chicago, Illinois. He served as a member of the Advisory Committee to the Commission's Institutional Investor Study and as Director of the Commission's Special Study of Securities Markets. His law firm is general counsel to the Midwest Stock Exchange, Inc., the Chicago Board Options Exchange, Inc. and the Options Clearing Corporation.

Aaron R. Eshman is President and Chief Executive Officer of Stern, Frank, Meyer & Fox, Inc., Los Angeles, California. He is also a former Governor of the American Stock Exchange and a Director and Executive Committee Member of the Securities Industry Association.

Robert M. Fomon is President and Chief Executive Officer of E. F. Hutton & Company Inc., New York, New York. He is also a former Chairman of the Pacific Stock Exchange.

John P. Guerin, Jr. is Chairman of New America Fund, Inc., and Mitchum, Jones & Templeton, Incorporated, Los Angeles, California. He is a former Chairman of the Pacific Stock Exchange and serves as Director of a number of public companies.

James H. Lorie is Professor of Business Administration at the Graduate School of Business of the University of Chicago. He was the author of the U. S. Treasury Department's statement on "Public Policy for American Capital Markets", submitted in February 1974 and is a former Governor of the National Association of Securities Dealers, Inc.

C. Rader McCulley is President of First Southwest Company, Dallas, Texas. He has served on various committees of the National Association of Securities Dealers, Inc. and has been a member of its Board of Governors. He has also been a member of the Commission's Advisory Committee on a Model

Compliance Program for Broker-Dealers and the Advisory Committee on the Implementation of a Central Market System.

Donald B. Marron is President and Chief Executive Officer of Mitchell, Hutchins, Inc., New York, New York. He is also a Director of the New York Stock Exchange and a Director of the Securities Industry Association.

Joane H. Miller is an individual investor residing in North Redington Beach, Florida. She attended the University of Tennessee and is a graduate of the New York Institute of Finance. She has been a registered representative of a New York Stock Exchange member firm and currently serves as Treasurer of two Florida Gulf Coast Symphony Boards.

James W. North is Executive Vice President of the Chase Manhattan Bank, N.A., New York, New York. He is a former President of the Trust Division of the New York State Bankers Association and President of the Trust Division of the American Bankers Association.

George Putnam is Chairman and President of the Putnam Funds and Chairman of the Putnam Management Company, Inc., Boston, Massachusetts. He is also the Treasurer of Harvard University and Chairman of the Harvard Management Company.

Ralph S. Saul is Chairman, President and Chief Executive Officer of INA Corp. , Philadelphia, Pennsylvania. Previously, he was Chairman of the Executive Committee of the First Boston Corporation and President of the American Stock Exchange. He was also Director of the Commission's then Division of Trading and Markets and a member of the Commission's Advisory Committee on Market Structure.

John J. Scanlon is a retired Executive Vice President and Chief Financial Officer of the American Telephone and Telegraph Co., New York, New York. He serves as Director of a number of public corporations including Avis, Inc., Browning-Ferris Industries, Inc., Harvey Hubbell, Inc., National Distillers and Chemical Corp., and USLIFE Corp. He is also Adjunct Professor of Finance at the Wharton Graduate School of Business of the University of Pennsylvania.

Donald Stone is a senior partner of Lasker, Stone and Stern, New York, New York, specialists on the New York Stock Exchange. He has served on the Advisory Committee to the Commission's Institutional Investor Study and as a member of the Commission's Advisory Committee on Market Disclosure and Advisory Committee on the Implementation of a Central Market System.

Robert W. Swinarton is Vice Chairman of Dean Witter & Co., New York, New York. He is also Chairman of the Board of Governors and Chairman of the

Executive Committee of the National Association of Securities Dealers, Inc. and Chairman of the Board of NASDAQ, Inc.

Donald E. Weeden is Chairman of the Board of Weeden & Co., New York, New York. He was a member of the Commission's Advisory Committee on Market Disclosure. Weeden & Co., which is a member of most regional stock exchanges, is the leading third market firm, and is the only registered odd-lot dealer on the Cincinnati Stock Exchange. Weeden & Co. also owns a substantial share of Institutional Network Systems (Instinet).

## APPENDIX C

### Section 11A(a)(1) of the Securities Exchange Act of 1934

Sec. 11A(a)(1) The Congress finds that -

(A) The securities markets are an important national asset which must be preserved and strengthened.

(B) New data processing and communications techniques create the opportunity for more efficient and effective market operations.

(C) It is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure --

(i) economically efficient execution of securities transactions;

(ii) fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets;

(iii) the availability to brokers, dealers, and investors of information with respect to quotations for end transactions in securities;

(iv) the practicability of brokers executing investors' orders in the best market; and

(v) an opportunity, consistent with the provisions of clauses (i) and (iv) of this subparagraph, for investors' orders to be executed without the participation of a dealer.

(D) The linking of all markets for qualified securities through communication and data processing facilities will foster efficiency, enhance competition, increase the information available to brokers, dealers, and investors, facilitate the offsetting of investors' orders, and contribute to best execution of such orders.

## APPENDIX D

### National Market Advisory Board Staff

Martin L. Budd, Executive Director, is a graduate of Dartmouth College; Worcester College, Oxford, which he attended on a Marshall Scholarship; and Harvard Law School, where he was an Editor of the Law Review. For the eight years prior to becoming Executive Director of the Board, he was associated with a New York law firm.

James P. Cullen, Special Counsel, is a graduate of the Johns Hopkins University, the University of Madrid and the University of Pennsylvania Law School. He was Data Processing Coordinator and a Trust Officer of Union First National Bank of Washington, D.C. He joined the Commission staff in May, 1973 in the Division of Market Regulation and was Special Counsel to the Office of Policy Planning prior to joining the Board staff.

Robert R. Wolf, Senior Adviser, is a graduate of Yale College. He was Assistant Vice-President of the Supreme Sugar Refinery Division of J. Aron & Co., Inc., New Orleans and a General Partner of Kohlmeyer & Co. He joined the Commission staff in December, 1973 as a Policy Planning Specialist and was Regional Office Coordinator prior to joining the Board staff.

Rhoda S. Clavan, Staff Assistant, joined the Commission staff in 1942. After a leave of absence, she returned in 1961 as Secretary to the Chief Counsel of the Special Study of Securities Markets. Prior to joining the Board staff she was Confidential Assistant to former Chairmen Cohen, Budge, Casey and Garrett.

In addition, the following member of the Commission staff has assisted the Board and its staff on a part time basis.

Thomas G. Kaplan, Attorney-Adviser, is a graduate of Harvard College and Harvard Law School. He joined the Commission staff in October, 1974 in the Division of Market Regulation.

## APPENDIX E

### National Market Advisory Board Technical Consultants

Donald H. Brown  
Senior Vice President  
Paine Webber Jackson & Curtis Incorporated

Norman Epstein  
Senior Vice President  
E. F. Hutton & Company Inc.

Robert C. Hall  
Chairman of the Board and President  
Securities Industry Automation Corporation

Richard Sbarbaro  
Vice President  
Midwest Stock Exchange Incorporated

Thomas E. McInerney  
President  
A.D.P. Financial Data Services

Stewart Monchik  
President  
Monchik-Webber Associates Inc.

Robert Parker  
Vice President  
Merrill Lynch Pierce Fanner & Smith Incorporated

Peter Mastrangelo  
Vice President  
Kidder, Peabody & Co. Incorporated

Thomas Schneider  
Senior Vice President  
Dean Witter & Co. Incorporated

C. Richard Justice  
Senior Vice President  
National Association of Securities Dealers Inc.

APPENDIX F

Securities and Exchange Commission  
Washington, D.C. 20519

Securities Exchange Act of 1934  
Release No. 11851  
November 19, 1975

Request by the National Market Advisory Board for Public Comment Regarding  
the Establishment of a National Market System

At the request of the National Market Advisory Board (the "Board"), the Securities and Exchange Commission today published the Board's "Request for Public Comment Regarding the Establishment of a National Market System."

The Commission wishes to note that this Request is being made by the Board and that the Commission is simply making available its facilities to assist the Board in soliciting public comment.

By the Commission

George A. Fitzsimmons  
Secretary F2

NATIONAL MARKET ADVISORY BOARD

Request for Public Comment Regarding the Establishment of a National Market  
System

The National Market Advisory Board (the "Board") was established by the Securities and Exchange Commission (the "Commission") on September 30, 1975. The Commission was directed to establish the Board by Section 11A(d)(1) of the Securities Exchange Act of 1934, as added by the Securities Acts Amendments of 1975, Pub. L. No. 94-29.

Sections 11A(d)(3)(A) and (B) of the Securities Exchange Act give the Board the following responsibilities:

"(3)(A) The Advisory Board shall study and make recommendations to the Commission as to the steps it finds appropriate to facilitate the establishment of a national market system. In so doing, the Advisory Board shall assume the responsibilities of any advisory committee appointed to advise the Commission, with respect to the national market system which is in existence at the time of the establishment of the Advisory Board."

“(B) The Advisory Board shall study the possible need for modifications of the scheme of self-regulation provided for in this title so as to adapt it to a national market system, including the need for the establishment of a new self-regulatory organization (hereinafter in this section referred to as a “National Market Regulatory Board” or “Regulatory Board”) to administer the national market system. In the event the Advisory Board determines a National Market Regulatory Board should be established, it shall make recommendations as to:

“(i) the point in time at which a Regulatory Board should be established;

“(ii) the composition of a Regulatory Board;

“(iii) the scope of the authority of a Regulatory Board;

“(iv) the relationship of a Regulatory Board to the Commission and to existing self-regulatory organizations; and

“(v) the manner in which a Regulatory Board shall be funded.

“The Advisory Board shall report to Congress on or before December 31, 1976, the results of such study and its recommendations, including such recommendations for legislation. as it deems appropriate.”

Section 11A(d)(3)(C) of the Securities Exchange Act further provides that, in carrying out its responsibilities, “the Advisory Board shall consult with self-regulatory organizations, brokers, dealers, securities information processors, issuers, investors, representatives of Government agencies, and other persons interested or likely to participate in the establishment, operation, or regulation of the national market system.”

The Board takes note of the fact that a number of commentators have recently made public their views with regard to a national market system. The Board now wishes to request formally that all interested parties furnish views to the Board with regard to the establishment, operation, or regulation of a national market system.

Submissions to the Board may include complete proposals for a national market system or partial proposals with respect to one or more elements of a national market system. Among the various elements that the Board intends to consider are: a composite limit order book, market-making, membership and access, trading rules, clearance and settlement, role of issuers, and administration and governance. The Board is particularly interested in suggestions as to the specific steps which should be taken to facilitate the establishment of a national market system, the timing of those steps and where appropriate, income and expense considerations. The Board is also interested in receiving comments with regard

to the statements and conclusions of the Securities and Exchange Commission's Advisory Committee on the Implementation of a Central Market System.

Submissions should be made to Andrew P. Steffan, Executive Secretary of the National Market Advisory Board, Securities and Exchange Commission, Washington, D.C. 20549, if possible, prior to March 1, 1976. The Board will also consider proposals received after this date, but urges that submissions be made as soon as possible. The Board also wishes to point out that it expects to commence consideration of these matters prior to receipt of outside comments.

Copies of all submissions will be made available for examination at the Commission's Office of Public Reference, File No. S7-602. The Board will consider, at a future date, the possibility of providing time for oral presentations by those persons who have made written submissions. Those interested in making oral presentations should notify the Executive Secretary.

## APPENDIX C

### LIST OF SUBMISSIONS TO NATIONAL MARKET ADVISORY BOARD

\*Date of original submission. Further comments, amplifications, replies to comments of others received but not listed by date.

#### SELF-REGULATORY ORGANIZATIONS

American Stock Exchange -- 6/25/76  
Boston Stock Exchange -- 5/28/76\*  
Chicago Board Options Exchange -- 5/3/76  
Cincinnati Stock Exchange -- 6/17/76  
Midwest Stock Exchange -- 6/15/76  
National Association of Securities Dealers -- 4/12/76  
New York Stock Exchange -- 7/1/76\*  
Pacific Stock Exchange -- 9/1/76  
Philadelphia Stock Exchange -- 7/28/76

#### BROKER-DEALERS

Boston Institutional Services Inc. -- 6/21/76  
The Chicago Corp. -- 7/27/76  
Merrill Lynch, Pierce Fenner & Smith Inc. -- 10/16/75  
Todd, William (Kuhn, Loeb & Co.) -- 7/22/76  
Weeden Holding Corp. -- Undated

#### ASSOCIATIONS

American Society of Corporate Secretaries -- 7/29/76  
Committee of Publicly Owned Companies -- 6/28/76  
Institutional Advisory Committee of the NYSE -- 8/17/76  
National Association of Investment Clubs -- 2/2/76  
National Market Association -- 12/8/76  
National Security Traders Association -- 6/3/76  
National Investor Relations Institute -- 3/15/76  
Regional Firms' Advisory Committee -- 12/15/76  
Securities Industry Association -- 6/3/76

#### GOVERNMENT AGENCIES

Comptroller of the Currency -- 6/8/76  
Department of Justice -- 6/14/76  
Securities Investor Protection Corp. -- 2/24/76

#### SECURITIES INFORMATION PROCESSORS

AutEx, Inc. -- 2/13/76  
Bunker-Ramo Information Systems Division -- 1/29/76 \*  
GTE Information Systems, Inc. -- 1/30/76 \*  
Institutional Networks Corp. (Instinet) -- 11/11/76  
Reuters Ltd. -- 3/1/76  
Securities Industry Automation Corp. -- 6/24/76

#### CLEARANCE AND SETTLEMENT ENTITIES

Boston Stock Exchange Clearing Corp. -- 5/28/76  
TAD Depository Corp. -- 7/15/76

#### ACADEMIC

Mendelson, Morris (U. of Penn-Wharton School) -- 3/2/76  
Ratner, David (Cornell University) -- 6/18/76  
Smidt, Seymour (Cornell University) -- 7/15/76

#### OTHERS

Batterymarch Financial Management Corp. -- 3/4/76  
1st National Bank of Boston -- 3/24/76  
Security Pacific National Bank -- 4/22/76  
R. Shriver Associates (Peake-Mendelson-Williams) -- 4/30/76 \*  
Stillman, Stanley -- 6/8/76

#### Comments on In-House Crosses Only

Allstate Insurance Co. -- 8/13/76  
Association for Preservation of Auction Markets -- 5/18/76  
Delaware Trust Co. -- 8/30/76  
Illinois Municipal Retirement Fund -- 8/6/76  
Merchants National Bank & Trust Co. of Indianapolis -- 8/9/76  
New York Stock Exchange -- 7/9/76

## APPENDIX H

### Section 17(d) (1) of the Securities Exchange of 1934

17(d) (1) The Commission, by rule or order, as it deems necessary or appropriate in the public interest and for the protection of investors, to foster cooperation and coordination among self-regulatory organizations, or to remove impediments to and foster the development of a national market system and national system for the clearance and settlement of securities transactions, may--

(A) with respect to any person who is a member of or participant in more than one self-regulatory organization, relieve any such self-regulatory organization of any responsibility under this title (i) to receive regulatory reports from such person, (ii) to examine such person for compliance, or to enforce compliance by such person, with specified provisions of this title, the rules and regulations thereunder, and its own rules, or (iii) to carry out other specified regulatory functions with respect to such person, and

(B) allocate among self-regulatory organizations the authority to adopt rules with respect to matters as to which, in the absence of such allocation, such self-regulatory organizations share authority under this title.

In making any such rule or entering any such order, the Commission shall take into consideration the regulatory capabilities and procedures of the self-regulatory organizations, availability of staff, convenience of location, unnecessary regulatory duplication, and such other factors as the Commission may consider germane to the protection of investors, cooperation and coordination among self-regulatory organizations, and the development of a national market system and a national system for the clearance and settlement of securities transactions. The Commission, by rule or order, as it deems necessary or appropriate in the public interest and for the protection of investors, may require any self-regulatory organization relieved of any responsibility pursuant to this paragraph, and any person with respect to whom such responsibility relates, to take such steps as are specified in any such rule or order to notify customers of, and persons doing business with, such person of the limited nature of such

self-regulatory organization's responsibility for such person's acts, practices, and course of business.