

MEMO# 2026

July 16, 1990

INSTITUTE COMMENTS ON NASD PROPOSED AMENDMENTS CONCERNING CONFLICTS OF INTEREST

July 16, 1990 TO: SEC RULES MEMBERS NO. 50-90 RE: INSTITUTE COMMENTS ON NASD
PROPOSED AMENDMENTS CONCERNING CONFLICTS OF INTEREST

The NASD recently proposed amendments to Schedule E of its By-laws, which regulates the potential conflicts of interest that exist when an NASD member participates in the public distribution of its own securities or the securities of an affiliate. The proposed amendments would apply the provisions of Schedule E to any public distribution of the securities of an issuer when a member that proposes to participate in the distribution or its associated persons, parent, or affiliates own 10 percent or more of the debt, preferred stock or of the combined voting and nonvoting common stock of an issuer. When Schedule E was first adopted, the NASD exempted investment companies by excluding them from the definition of "affiliate". However, the proposed amendments expand the coverage of Schedule E to conflicts of interest between the member firm and the issuer which are deemed to exist when the member owns more than 10 percent of the debt or equity of the issuing company. Thus, literally read, the proposed amendments would apply to the distribution of investment company shares. In its comment letter, the Institute requested the NASD to clarify that the proposed changes were not intended to cover investment companies. The Institute noted that the drafters of Schedule E intended to exclude investment companies and that there is no justification to repeal or modify this exclusion. Any change in the investment company exclusion would require a complete revamping of the way in which investment company shares are currently distributed. We also explained that conflicts of interest involving investment companies are already regulated under the Investment Company Act. Attached is a copy of the Institute's comment letter and the proposed changes to Schedule E. We will keep you informed of developments. Amy B. Rosenblum Assistant General Counsel Attachment