

**MEMO# 7388**

November 3, 1995

# **PROPOSED NASD INTERPRETATION CONCERNING SUITABILITY OBLIGATIONS TO INSTITUTIONAL CUSTOMERS**

November 3, 1995 TO: SMALL FUNDS COMMITTEE No. 19-95 RE: PROPOSED NASD  
INTERPRETATION CONCERNING SUITABILITY OBLIGATIONS TO INSTITUTIONAL CUSTOMERS

The National Association of Securities Dealers, Inc., recently filed with the Securities and Exchange Commission a proposed interpretation of the suitability obligations of NASD members to institutional customers. A copy of the proposal is attached. The comment period on the proposal ends on November 14, 1995. Please provide me with any comments on the NASDs proposal by Wednesday, November 8, 1995. The interpretation states that the two most important considerations in determining the scope of a members suitability obligations in making recommendations to an institutional customer are the customers capability to evaluate investment risk independently and the extent to which the customer intends to exercise independent judgment in evaluating a members recommendation. The interpretation states, "Where the broker-dealer has reasonable grounds for concluding that the institutional customer is making independent investment decisions and is capable of independently evaluating investment risk, then a members obligation to determine that a recommendation is suitable for a particular customer is fulfilled." The interpretation lists various considerations relevant to a determination of an institutional customers capability to evaluate investment risk independently. These considerations include the use of an investment adviser or other consultant. The interpretation states that while it is potentially applicable to any institutional customer, it "is more appropriately applied to an institutional customer with at least \$10 million invested in securities in the aggregate in its portfolio and/or under management." Thomas M. Selman Associate Counsel Attachment