

MEMO# 4898

June 23, 1993

NASD PROPOSES AMENDMENTS TO FREE-RIDING AND WITHHOLDING INTERPRETATION

June 23, 1993 TO: CLOSED-END FUND COMMITTEE NO. 17-93 COMPLIANCE COMMITTEE NO. 12-93 INVESTMENT ADVISERS COMMITTEE NO. 15-93 SEC RULES COMMITTEE NO. 55-93 RE: NASD PROPOSES AMENDMENTS TO FREE-RIDING AND WITHHOLDING INTERPRETATION

The NASD has proposed amendments to the Free-Riding and Withholding Interpretation of the Board of Governors under Article III, Section 1 of its Rules of Fair Practice. The proposed amendments were developed by a special committee (the Free-Riding Committee) established to determine if the Interpretation's restrictions, definitions and obligations are relevant in today's securities markets. Attached is Special NASD Notice to Members 93-40, dated June 15, 1993, which includes the full text of the Interpretation and the proposed amendments thereto. The purpose of the Interpretation is to protect the integrity of the markets by ensuring that NASD members make a bona fide public distribution of "hot issue" securities and neither withhold such securities for their own benefit nor use the securities to reward other persons in a position to direct future business to the member. "Hot issues" are defined as securities of a public offering that trade at a premium in the secondary market when such trading commences. The Interpretation restricts member sales of hot-issue securities to the accounts of specified categories of persons including, among others, senior officers of registered investment companies, registered investment advisory firms, and any other persons within such organizations whose activities influence or include the buying or selling of securities. Investment companies registered under the Investment Company Act of 1940 are expressly excluded from the categories of persons to whom member firms are prohibited from selling hot-issue securities. The Free-Riding Committee has proposed amendments to specific provisions of the Interpretation and requested comment on whether other parts of the Interpretation should be amended. Among other things, an amendment has been proposed to exempt from the categories of restricted persons individuals with limited purpose registrations, such as persons registered as representatives or principals in registration categories limited to investment company securities. Comment is requested on the propriety of adopting such an exemption and, if appropriate, the proper scope of the exemption. In addition, comment is requested on whether foreign mutual funds which are subject to a similar scheme of regulation as that governing domestic funds should be exempted from the restricted persons categories and, if so, the proper scope of such an exemption and the appropriate methodology for determining the similarity of regulation. Comment is also solicited on the types of securities that should be covered by the Interpretation. The Interpretation currently applies to both equity and debt securities. Comment is solicited on whether the Interpretation should be applied to "straight" debt

securities and whether "rated" debt should be excluded from the Interpretation. In the discussion of the scope of the Interpretation's coverage, it is noted that the Free-Riding Committee believes that shares of closed-end investment companies should remain covered by the Interpretation. Comments on the proposed amendments are due to the NASD by July 31, 1993. If you have any comments on the specific proposed amendments or on the Interpretation generally, please provide them to me by July 21, 1993. My direct number is 202/955-3523. Amy B.R. Lancellotta Associate Counsel Attachment

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.