

ASD ▪ NASDAQ ▪ NASD MARKET SERVICES ▪ NASDAQ INTERNATIONAL

National

Association of

Securities

Dealers

Inc.

ABOUT THE NASD

The National Association of Securities Dealers, Inc., is the not-for-profit, self-regulatory organization for the over-the-counter securities market. More than 6,700 broker-dealers—or virtually all firms in the nation that do a securities business with the public—belong to the NASD and agree to abide by its rules as a condition of membership. More than 450,000 employees of these firms are registered with the NASD.



Through its self-regulatory activities and the activities of its subsidiary organizations—NASDAQ, Inc., NASD Market Services, Inc., and NASDAQ International, Ltd.—the NASD seeks to facilitate efficient domestic and international financial markets for the benefit of investors, NASDAQ companies, and NASD member firms.

In keeping with the true spirit of self-regulation, the NASD is governed by a member-controlled Board of Governors. Through a nationwide system of committees, the NASD conducts peer reviews of members' actions, develops rules and regulations, and designs new services for the market.

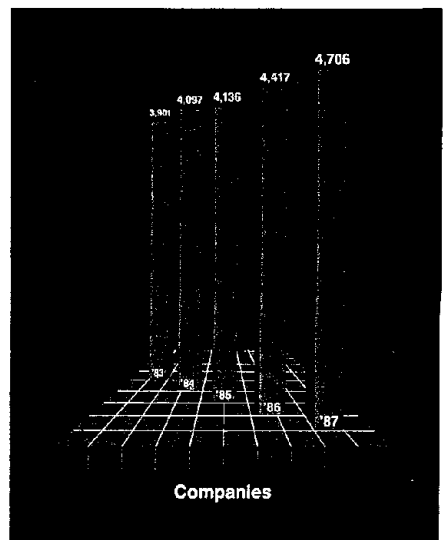
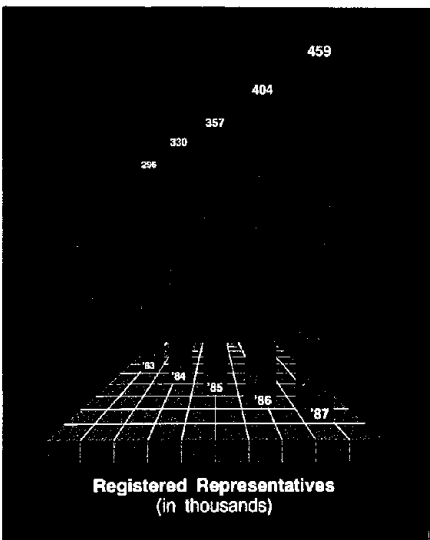
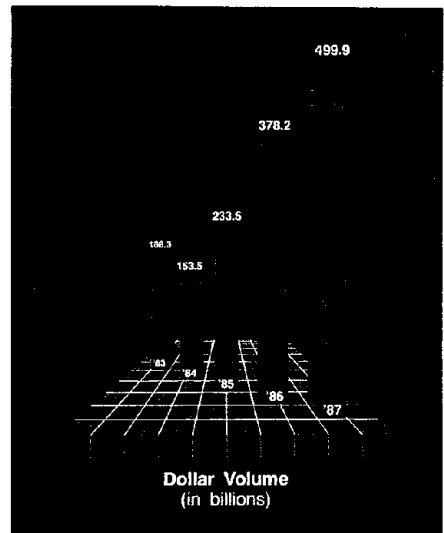
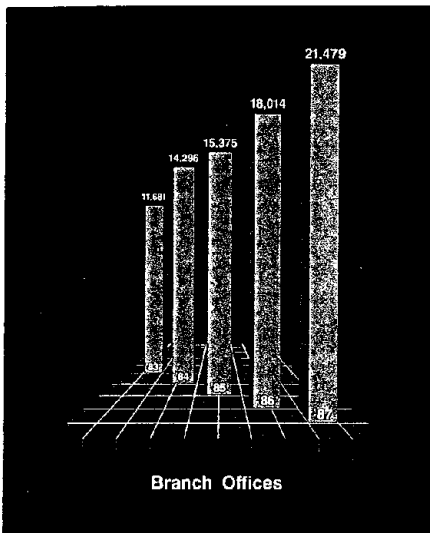
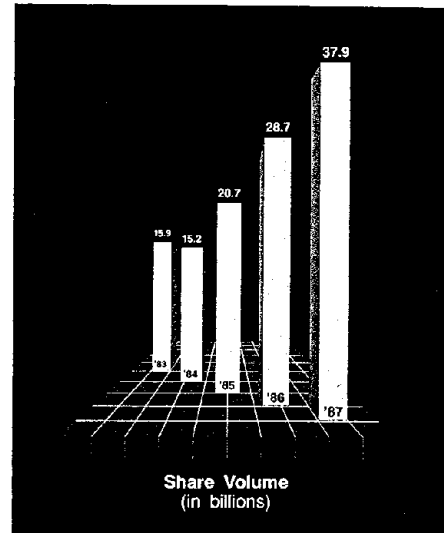
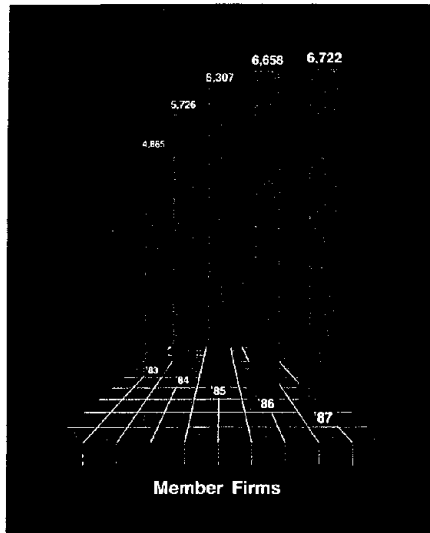
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IVE-YEAR REVIEW

NASD

NASDAQ



1987 KEY FACTS AND FIGURES

- Chairman of the Board Joseph R. Hardiman succeeds Gordon S. Macklin as the NASD President. James M. Davin assumes the Chairmanship.
- Membership in the NASD grows to 6,722 firms operating 21,479 branch offices and employing 459,000 registered representatives—all at the highest levels in the NASD's 48-year history.
- NASDAQ volume reaches 37.9 billion shares in 1987, with a dollar volume of \$500 billion—a 32 percent increase over 1986. During the past decade, NASDAQ volume has increased twenty-fold.
- Regulatory staff in the Legal and Compliance Division grows to more than 850 persons. Examinations of members, market surveillance actions, qualifications examinations, dollar volume of corporate financing reviews, advertising reviews, and arbitration claims all break records.
- The Central Registration Depository for registered representatives extends its services to all 50 states and prepares to process broker-dealer firm registrations and renewals.
- To serve the market's continuing growth, the NASDAQ System is upgraded to a 450-million-shares-a-day capacity. The Rockville, Maryland, disaster-recovery site functions successfully.
- The NASD introduces a third generation of NASDAQ terminals for traders and financial institutions, with new customized functions and four times the speed of existing terminals.
- To overcome the telephone bottlenecks found during the October 19–23 market break, the NASD Board proposes strengthening the Small Order Execution System and develops the Order Confirmation Transaction service to facilitate access to market makers. The “Report of the Presidential Task Force” characterizes the NASD's actions as “swift and dramatic.”
- The Securities and Exchange Commission approves corporate governance requirements for NASDAQ National Market System companies. Maine, Nevada, Oklahoma, and Wisconsin join the states exempting NASDAQ/NMS securities from registration under state blue-sky laws.
- Internationally, overseas terminals with NASDAQ data increase by 50 percent, transaction information and more securities further enhance the London link, Level 2/3 service becomes available to NASD members in the United Kingdom, and the first stage of a NASDAQ-Singapore link begins.
- NASDAQ International opens in London to support NASD members in London and serve as a liaison to U.K. and European companies seeking to list securities on NASDAQ.

HAIRMAN'S AND PRESIDENT'S REPORT



Joseph R. Hardiman (left), NASD President, and James M. Davin, 1987 NASD Chairman.

In the last decade, the NASD experienced unprecedented growth: Membership jumped from 2,772 firms in 1977 to 6,722 in 1987 . . . The number of branches more than tripled, surging from 6,144 to 21,479 . . . The number of registered representatives soared from 192,000 to 459,000 . . . The NASDAQ market expanded from 2,456 companies and 2,575 securities to 4,706 companies and 5,537 securities . . . Share volume and dollar volume increased 20 times—from 1.9 billion shares to 37.9 billion, and from \$25 billion to \$500 billion.

In 1987, investor protec-

tion, quality-of-market issues, and improved services continued as our principal agenda items.

In a major expansion of its regulatory responsibilities, the NASD in July 1987 began monitoring and inspecting some 70 previously unregulated firms that are active in the U.S. government securities market. The authority to examine these firms was conferred upon the NASD by the Government Securities Act of 1986.

Throughout the year, we also took steps to expand our surveillance capabilities and programs to embrace the "pink sheet" market, in which an estimated 11,000 non-NASDAQ OTC stocks are traded. We await SEC approval of our proposals to require the daily reporting by members of transaction information in these securities.

The field of investment advisers and financial planners is diverse and largely obscure, according to our studies. After completing a pilot program in which we examined registered investment advisers who are already associated with the NASD, we advised the SEC that the NASD is prepared to become the self-regulatory organization for such persons.

At the apex of our investor protection activities is the work of the Regulatory Review Task Force, which was formed in April 1987 to undertake a comprehensive review of the NASD's regulatory policies, practices, and procedures. Chaired

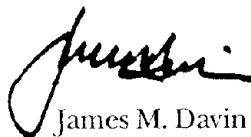
by A. A. Sommer, Jr., a noted securities lawyer and former SEC Commissioner, the task force will deliver its report—complete with recommendations—to the NASD Board in the spring of 1988.

The NASD's Arbitration Program, established in 1968 to help investors resolve disputes with their broker dealers, has grown nine-fold in the 1980s. We are making qualitative improvements to the program and, through a major staff expansion, are gearing up to handle a burgeoning caseload resulting from the 1987 Supreme Court ruling in the *McMahon* case and the aftermath of the market break.

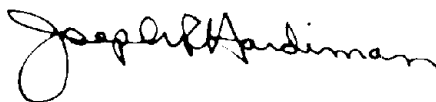
In the NASDAQ market, a series of major initiatives were begun in 1987: We took the lead among all markets for a uniform rule on shareholder voting rights . . . After the October market break, we hastened to make the Small Order Execution System (SOES) more efficient and reliable for individual investors . . . We began building a limit-order file in SOES . . . For the better execution and post-execution processing of larger orders, we devised new automated services . . . For the benefit of issuers and investors, we mandated the corporate governance standards of enlightened NASDAQ/NMS companies and urged the SEC to adopt rules to prohibit shorting into secondary distributions . . . We actively supported education for and about the financial services industry.

In response to the events of October, we created a special committee of the Regulatory Review Task Force to examine the structure and mechanics of the NASDAQ market. Irving M. Pollack, a former SEC Commissioner and a 33-year veteran of that agency, heads the committee.

An era in the NASD's history came to a close in mid-1987, when Gordon S. Macklin moved from the Presidency he had held for 17 years to the chairmanship of a prominent member firm. His service is reflected in the name of our Maryland operations center, the Gordon S. Macklin Building, and in every aspect of the NASD's ongoing work.



James M. Davin
1987 Chairman



Joseph R. Hardiman
President

ASD—THE YEAR IN REVIEW

For securities firms, regulators, and investors alike, 1987 proved to be a year of challenge and change. To meet these challenges, the NASD moved to strengthen the quality of its services and the NASDAQ market.

Three years ago, the NASD inaugurated the Small Order Execution System (SOES) for the automatic, computer-to-computer execution of customer orders of 1,000 shares or less without the usual telephone call between buyer and seller. SOES was designed to serve the individual investor and to save brokers and market makers time in the execution of small orders.

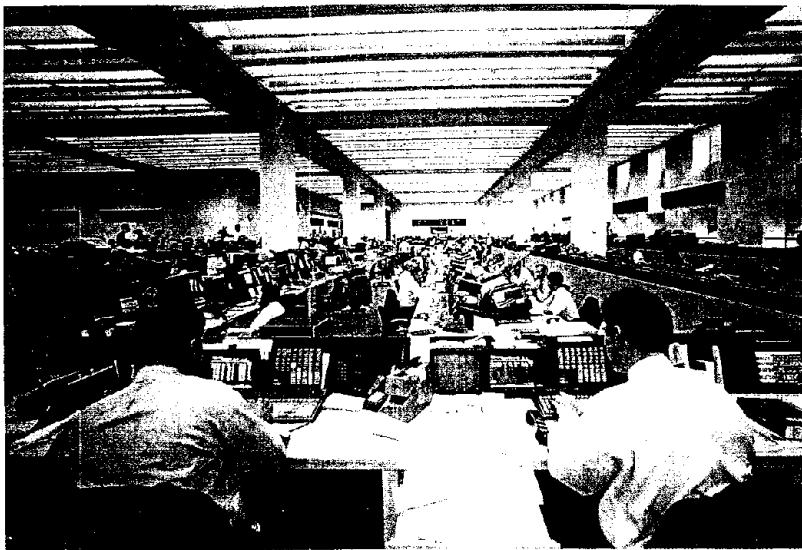
The hectic events of October 1987 demonstrated a need to increase usage of SOES. On November 16th, less than one month after the break, the NASD

became the first stock market to take steps to enhance market capacity and efficiency. The NASD Board approved several changes in SOES to significantly increase the number of customer orders executed over the computer, without the use of telephones. These and other planned improvements will help ensure that investors have efficient access to the NASDAQ market, especially during periods of high volume.

In commenting on the NASD's actions, the Presidential Task Force on Market Mechanisms, chaired by Nicholas F. Brady, said: "Had the proposed rules been in effect during the market break, it is possible, if not probable, that most of the problems encountered in the execution of small orders in the over-the-counter market would not have occurred."

Earlier in the year, the NASD approved another market enhancement—the construction of a limit-order file capability in SOES. The NASD Advisory Council, composed of the Chairmen of the 13 District Committees, strongly recommended this enhancement for the benefit of individual investors.

The limit-order file capability will permit SOES subscribers to enter limit orders that are reasonably related to the market. If the order cannot be executed immediately, SOES will hold it until the inside market reaches the limit price. When the NASDAQ inside market equals or betters the limit



NASDAQ's 545 market-making firms include large, national firms—such as Merrill Lynch, Pierce, Fenner & Smith Incorporated (above)—regional firms, and local firms. The typical stock in NASDAQ has an average of eight market makers.



price, the system will attempt to execute the order. This enhancement to the NASDAQ System is expected to go on-line in 1988.

In March 1987, the NASD Board proposed to the SEC the adoption of a uniform rule by each equity securities market that would emphasize the principle of equal shareholder voting rights but allow for legitimate exceptions. The 1987 discussion of the issue was triggered when the New York Stock Exchange applied to the SEC in September 1986 for permission to abandon its longstanding one-share, one-vote standard.

In May 1987, the NASD became the first self-regulatory organization to submit a share-

holder voting rights proposal to its membership. The rule was proposed in the form of a qualifications standard for domestic NASDAQ companies. The general premise of the rule is to prohibit issuers of NASDAQ securities from issuing any class of securities or taking any other corporate action that would nullify, restrict, or disparately reduce the per-share voting rights of holders of an outstanding class or classes of publicly traded securities of the issuer.

In the absence of a similar action by other major markets, the SEC published for comment a shareholder voting rights proposal of its own, modeled closely after the NASD proposal. The SEC took this action when after months of discussion it appeared that the major markets would not reach a consensus.

Gordon S. Macklin Building

In honor of its President from 1970 to 1987, the NASD named its computer facility in Rockville, Maryland, the Gordon S. Macklin Building.

Another system developed by the NASD to overcome the limitations of telephone contact, particularly in fast-moving markets, is the Order Confirmation Transaction (OCT) service. OCT enables member firms to direct orders—of any size for customer as well as for firm accounts—to a specific market maker via NASDAQ terminals, thereby bypassing the telephone. The recipient can accept or decline the order with a few simple keystrokes on the terminal.

Orders entered and accepted through OCT are automatically (1) confirmed via displays on the terminals of both the order-entry and market-making firms, (2) reported to the NASDAQ

System and distributed worldwide to information vendors, and (3) sent to the clearing corporation as locked-in trades. OCT became operational on January 15, 1988.

For the more complex, larger orders that require telephone negotiation to complete, the NASD is developing the Automated Confirmation Transaction (ACT) service for mid-1988 availability. ACT will permit the parties to a telephone negotiation to “lock-in” the post-execution steps involved in completing a transaction, i.e., transaction reporting, comparison, and clearance and settlement.

The use of ACT will be mandatory for domestic transactions and will have great utility for international dealing.

Alex. Brown & Sons, Inc., was among the first NASDAQ market-making firms to use NASDAQ's third generation of terminals—the new NASDAQ Workstation.™



In July 1987, the SEC approved mandatory corporate governance standards for NASDAQ National Market System (NMS) companies. The standards codify the existing practices of the great majority of companies and provide protection to their stockholders. New NASDAQ/NMS issuers are now required to maintain a minimum of two independent directors on their boards, have an audit committee with a majority of independent directors, hold annual shareholder meetings, conduct appropriate reviews of all related-party transactions, and meet other standards.

To allow time for companies that need to secure shareholder approval to achieve compliance, the new corporate governance standards will become effective on February 1, 1989, for issuers with securities on NASDAQ/NMS on August 4, 1987.

In response to a rulemaking petition of the NASD, the SEC published a proposal that would prohibit persons from covering short sales of a security with securities purchased from an offering by that issuer if such short sales were made during the time between the filing of a registration statement for the offering and the commencement of a stock distribution.

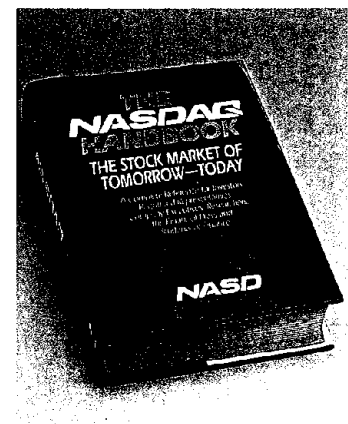
Because of the availability

of securities at a fixed price from an offering, the risks entailed in covering short sales in that issue are reduced substantially. To the extent that price reductions do not come from either anticipation of dilution, adverse news, or other market forces, the NASD believes this may adversely affect issuers in that the decrease in price deprives the issuer of offering proceeds that would have been realized had the market not been subject to such short selling.

The NASD petition was based upon recommendations by the NASD Corporate Advisory Board and its Corporate Financing Committee. It was also endorsed by former SEC Commissioner Irving M. Pollack in his July 1986 study entitled *Short-Sale Regulation of NASDAQ Securities*.

In April 1987, the NASD established its Regulatory Review Task Force, under the chairmanship of A. A. Sommer, Jr. The task force will report its findings and recommendations to the NASD Board in the first quarter of 1988. Among the areas under examination by the task force are:

- Increasing automation in the market surveillance process.
- Prevention and detection of improper sales/trading practices.
- Disciplinary procedures and enforcement policies.



The NASDAQ Handbook, written by corporate executives, investment professionals, and business journalists, features 30 chapters on the many facets of the NASDAQ market.

- Disclosures concerning the termination of sales personnel and principals.
- Qualification standards and examinations for both principals and registered representatives.
- Internationalization and inter-market surveillance.
- Cooperative programs with state/federal securities administrators.

In December 1987, the NASD Board established a special committee of the task force to analyze a number of structural and



A.A. Sommer, Jr. (left), Chairman of the Regulatory Review Task Force, and Irving M. Pollack, Chairman of the Special Committee to the Task Force, discuss the work of their committees.

quality-of-market issues. The committee is chaired by Irving M. Pollack and consists of representatives of individual investors, institutional investors, NASDAQ issuers, securities traders, and members of the academic community.

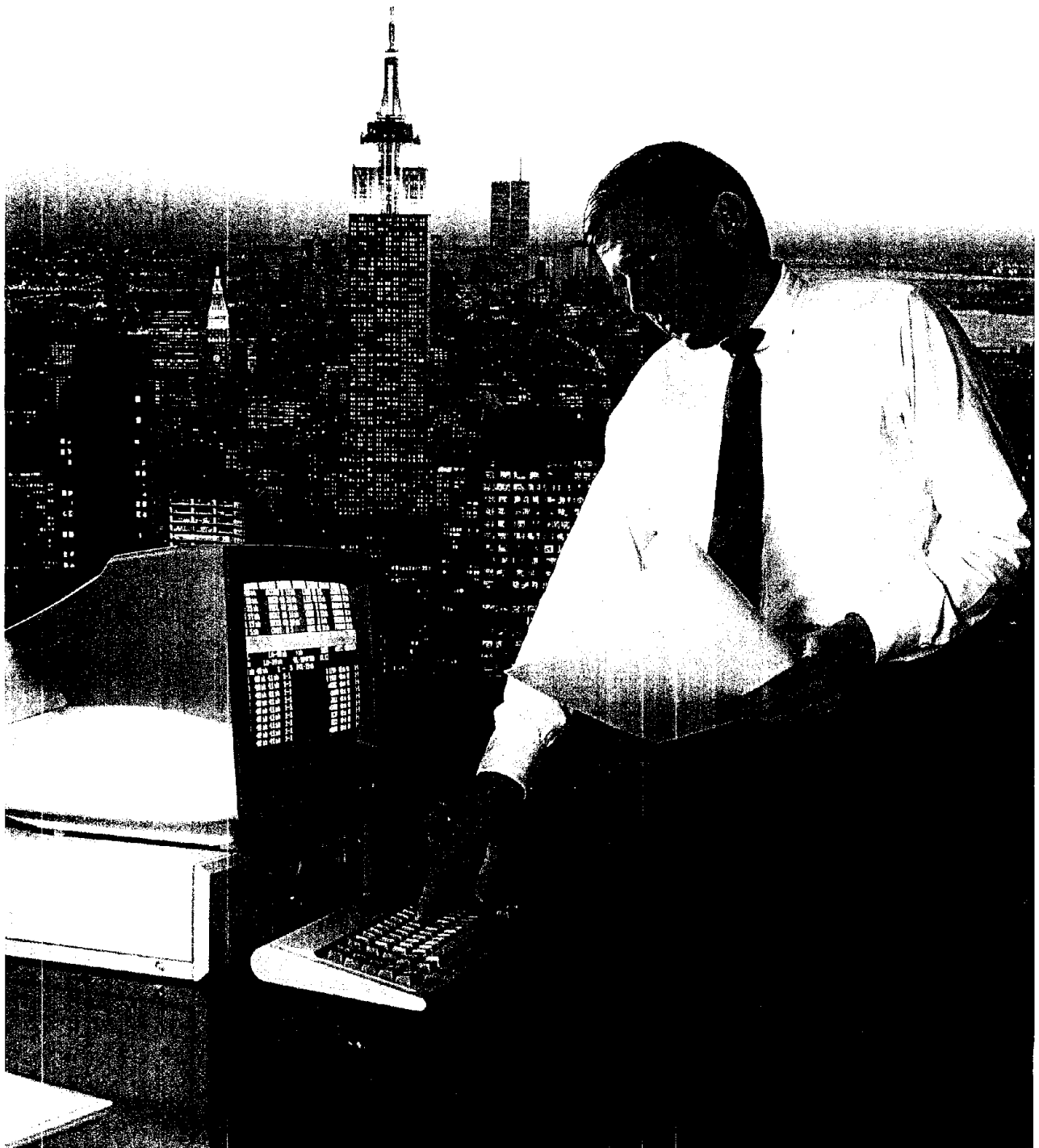
The issues to be studied by the special committee include:

- Standards for companies and market makers.
- Market-maker capital and obligations.
- Market liquidity.
- Adequacy of communications systems.
- The impact of international trading on the NASDAQ market.

The special committee, which is scheduled to report to the NASD Board in mid-1988, will help ensure that NASDAQ's market structure and systems anticipate investor needs in an increasingly demanding market environment.

The year 1987 was marked by new and expanded oversight into three different sectors: government securities dealers, non-NASDAQ securities, and investment advisers.

In July, the NASD assumed responsibility for monitoring and inspecting government securities dealers who transact their business in the largest securities market in the world. To fulfill its duties, the NASD integrated the firms into the membership, acquainted them with Treasury Department regulations and the NASD's role in their enforcement, developed examination procedures, and trained a special NASD staff of examiners and supervisors.



The NASD's third generation of terminals---the NASDAQ Workstation™---features faster, more powerful processing, market minding, limit alerts, and more.

In December, the NASD filed a proposal with the SEC that will require members to electronically report price and volume information for trades in an estimated 11,000 "pink sheet" issues on a daily basis. The NASD is also considering a requirement that members document their best-execution efforts in those issues, developing an expanded field examination program of members active in this area, and creating an electronic "OTC bulletin board" that would permit subscribers to access market makers' quotes and indications of interest in non-NASDAQ securities.

The Surveillance Department completed a one-year pilot program of examining registered investment advisers who are NASD members and volunteered for the program and a two-year study of financial planners/ investment advisers as a whole. The SEC's Division of Investment Management assisted in the effort.

The NASD Board agreed that the NASD would, if requested, become the self-regulatory organization for registered investment advisers who are members or persons associated with members. The request will have to come from the SEC, and it will be necessary to expand the NASD's authority by amending federal securities laws.

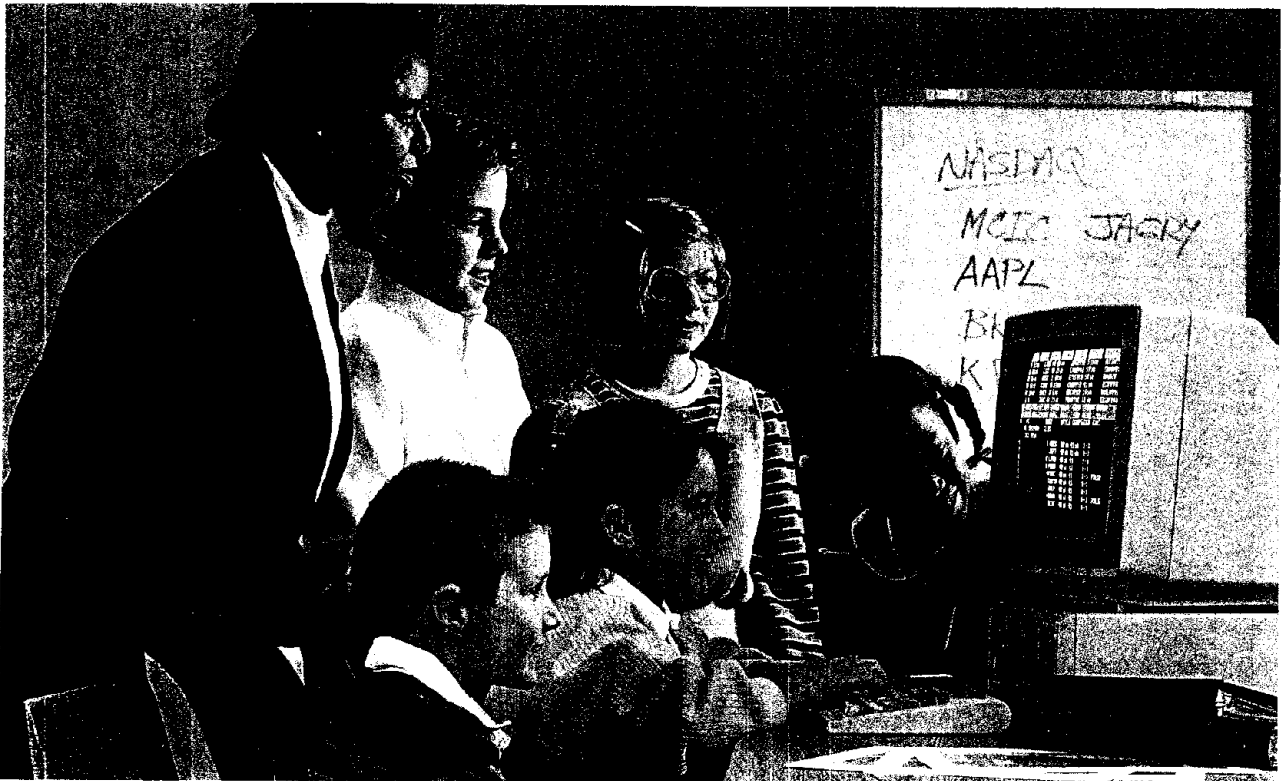
As a complement to its investor protection and quality-of-market endeavors, the NASD is supporting education for and about the financial services industry in the following ways:

■ *The NASDAQ Handbook.*

The first complete reference book on the NASDAQ market, *The NASDAQ Handbook: The Stock Market of Tomorrow—Today*, was compiled by the NASD and published in July 1987 by Probus Publishing Company, Chicago. The book chronicles NASDAQ's growth and

A \$9 million computer hardware upgrade at the Trumbull, Connecticut, and the Rockville, Maryland, facilities boosts NASDAQ System capacity to 450 million shares per day.





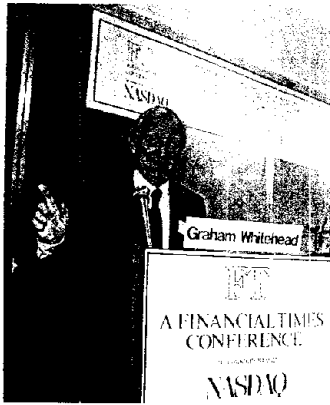
international dimension, providing investors with a comprehensive look at the current workings and future direction of the NASDAQ market. The handbook profiles NASDAQ market investors, provides an overview of NASDAQ companies, offers practical investment advice, and analyzes recent trends in liquidity, economic efficiency, trading characteristics, and market technology. Its 30 chapters, covering 577 pages, were contributed by corporate executives, scholars, journalists, consultants, and investment professionals.

■ *Stock Market Game.* For the 1987–1988 school year, more than 3,000 NASDAQ/NMS stocks have been added to the Securities Industry Association's Stock Mar-

ket Game, in which 400,000 secondary and elementary students in 44 states compete in a simulation exercise designed to enrich economic education. The NASD provides weekly prices on NASDAQ/NMS stocks, supplies teacher/student market guides, and provides financial support to the program. The SIA's Foundation for Economic Education, SIA members, Standard & Poor's Corporation, and many other groups also support the game.

■ *Center for Research in Security Prices.* Financed jointly by the NASD and Dimensional Fund Advisers, Inc., the Center for Research in Security Prices at the University of Chicago in 1987 established a comprehensive data base of historical prices for

When selecting their portfolios, the 400,000 students participating in the Stock Market Game can choose from more than 3,000 NASDAQ/NMS securities.



Graham H. Whitehead, President of Jaguar, plc, and member of the NASD Board of Governors, addresses participants at a joint NASDAQ/Financial Times conference in London on American Depository Receipts.

NASDAQ common stocks. The file contains daily information about trades, capitalizations, and returns to shareholders for all common stocks on NASDAQ since December 1972. It also includes periodic information on shares outstanding, stock splits, dividends paid, merger and liquidation information, name histories, SIC codes, CUSIP identifiers, and ticker symbols. This database opens new avenues for original research by the financial services industry and the academic community in examining the comparative characteristics of companies and the markets for their securities.

■ *Wharton School Conference.* In April, the Rodney L. White Center for Financial Research at the University of Pennsylvania devoted its annual seminar to the NASDAQ market. Participating in the conference were members of the academic community, industry executives, the financial press, and NASD officials.



The 1987 annual seminar of Wharton School's Rodney L. White Center for Financial Research focused exclusively on the NASDAQ market.

■ *Vanderbilt University Financial Markets Research Center.* In 1987, the NASD became a supporting member of the new financial markets research center established at the Owen Graduate School of Management, Vanderbilt University. The center fosters research to improve understanding of developments in financial markets, financial instruments, and financial institutions. Research on the NASDAQ market is expected to be one of the center's major undertakings. The NASD also continues subscribing memberships in the Rodney L. White Center at the Wharton School, the Salomon Brothers Center at New York University, and the American Assembly of Collegiate Schools of Business.

■ *John H. Hodges, Jr., Memorial Award.* John H. Hodges, Jr., a leader in the creation and growth of the NASDAQ market, died in November 1986. In April 1987, many of the friends he had made during his 33 years with the NASD established the John H. Hodges, Jr., Memorial Award at the Wharton School at the University of Pennsylvania, his alma mater. The award is presented annually to the outstanding Ph.D. student in finance at Wharton.

As part of its ongoing efforts to improve and strengthen its regulatory programs, the NASD in 1987 retained Nolan, Norton &

NASDAQ National Market System as they are reported.

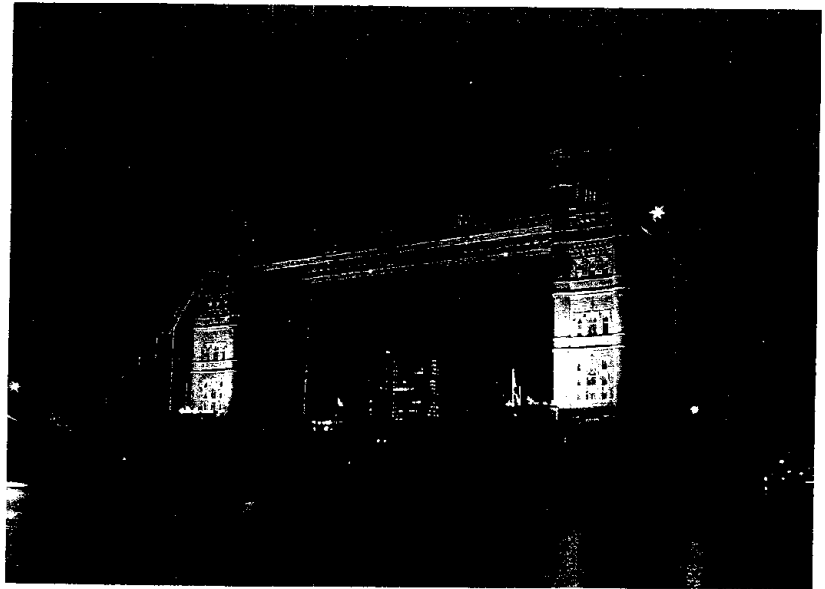
The automated symbol directory enables NASDAQ Level 2/3 subscribers to call up market-maker and issuer information. A fifth-character geographic identifier also allows subscribers to access telephone numbers of branch offices of market-maker firms.

RELIABLE SERVICE

The NASDAQ System's Central Computer Complex operated throughout 1987 with an uptime of 98.9 percent. The System experienced no downtime whatsoever during the week of October 19-23, when it processed 1.2 billion shares, 63 percent more than the weekly average in the first nine months of the year.

To keep pace with NASDAQ volume, the NASD boosted system capacity to 450 million shares per day and is planning for further expansion. A new generation of UNISYS processors was acquired to increase capacity at both the Trumbull, Connecticut, and the Rockville, Maryland, computer facilities. This \$9 million hardware upgrade also supports the NASDAQ Workstation™ terminal and other services.

NASDAQ's disaster-recovery and back-up system, the only system of its kind among major world securities markets, passed its first real-life test in December when a power-company outage shut down the main com-



puter facility in Trumbull. The Rockville facility bridged service until power was restored to the Trumbull site.

The back-up facility is designed to continue operation of the NASDAQ market in the event of a major outage at the Trumbull facility or at a major NASD communication facility.

During the week of November 9, the United Kingdom became a hub of international activity when the NASD opened an office in London, co-sponsored a conference on the ADR market with the *Financial Times*, and introduced Level 2/3 service to the U.K., permitting NASD members to make markets from outside the U.S.

The NASD's new London office—NASDAQ International—serves as a liaison to United Kingdom and European companies

To celebrate the opening of its new London office, NASDAQ International, Ltd., held a reception for 500 members of the financial community at London's Tower Bridge.



Of the 139 companies whose shares trade as American Depositary Receipts (ADRs) in the U.S., 97 are NASDAQ companies. Two of every three ADR shares traded in the U.S. are traded in the NASDAQ market.

seeking to list on NASDAQ directly or through an American Depositary Receipt. The London office also supports the growing number of NASD members in Europe.

The NASDAQ communications link with the SEAQ (Stock Exchange Automated Quotations) System in London, which has been in operation since April 1986, was expanded in 1987 to include quotations and transaction information on more than 700 securities from the two markets. Automatic intercontinental execution and trade confirmation over the link are scheduled to become available in 1989.

A trans-Pacific link between NASDAQ and the SESDAQ (Stock Exchange of Singapore Dealing and Automated Quotations) System became fully operational in March 1988, with a daily exchange of quotations on 35 NASDAQ securities traded in both markets.

Because the NASDAQ architecture offers a highly efficient technological response to the needs of international as well as domestic trading, NASDAQ is exploring additional linkages with other markets.

For trade comparison in the Eurobond market, NASDAQ is providing assistance to the Association of International Bond Dealers (AIBD) on a system called Trade Accounting and Reconciliation (TRAX). NASDAQ is designing a common communications front end that will enable TRAX and the NASD's proposed Automated Confirmation Transaction (ACT) service to be linked for international trade comparison.

In addition, the NASD has begun development of a centralized automated market for private placements.

A new NASDAQ-like system, called Private Offerings and Reciprocal Trading through Automated Linkages (PORTAL), will provide a highly regulated market for the trading by qualified investors of unregistered, world-class international securities meeting SEC conditions for exemption from the disclosure requirements under the Securities Act of 1933.

INVESTOR PROTECTION HIGHLIGHTS

■ The NASD's 14 District Offices conduct 4,672 examinations of main and branch offices and resolve 4,709 of the 5,335 customer complaints received.

■ As a result of 826 formal disciplinary actions ordered, the NASD's District Business Conduct Committees render 507 disciplinary decisions and accept 263 letters of acceptance, waiver and consent and 5 summary complaints. These actions lead to the expulsion of 17 firms, the barring of 169 individuals, the suspension of 9 firms and 94 individuals, and the imposition of \$2,250,000 in fines.

■ The NASD's automated market surveillance of NASDAQ trading triggers 19,775 on-line price and volume alerts, which lead to 249 formal investigations and the referral of 57 cases to the SEC.

■ The Market Surveillance Committee orders major disciplinary actions for market-related violations—including non-compliance with SOES rules, manipulation, and fraudulent mark-ups—and imposes penalties that include suspensions and fines totaling more than \$192,000.

■ The Corporate Financing Department reviews the underwriting terms of 3,200 corporate equity, debt, REIT, and direct participation program offerings with an aggregate volume of \$169 billion. These reviews result in the issuance of 500 no-objection letters, requests for more information in 2,300 cases, and letters objecting to the terms in 400 cases.

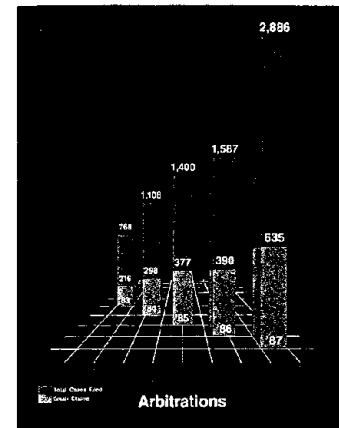
■ The Advertising Department reviews 32,500 pieces of advertising and sales literature, up 35 percent from 1986. Of these, about two thirds require revisions to comply with regulations.

■ Public customers, member firms, and associated persons file 2,886 arbitration claims with the NASD, an 82 percent increase over 1986, and request an aggregate of \$160 million in relief. The NASD closes 1,624 cases, a 43 percent increase over 1986. Of the cases decided by arbitrators, 58 percent are decided in favor of public customers.

■ To enhance investor information about industry malfeasance, the NASD increases disclosure of NASD disciplinary decisions and paves the way for further disclosure in 1988.

■ The Surveillance Department supervises the self-liquidation of 10 firms and the distribution of \$19 million to customers and broker-dealers.

■ The Qualifications Department administers 296,000 tests in 1987, up from 262,000 in 1986.



ASD BOARD OF GOVERNORS



To Serve Until January 1988

(seated left to right)

*WILSON C. WEARN
Multimedia, Inc.
Greenville, South Carolina

RONALD E. BUFSINGER
A.G. Edwards & Sons, Inc.
St. Louis, Missouri

RICHARD C. ROMANO
Romano Brothers and Company
Evanston, Illinois
NASD Vice Chairman, 1987

JOSEPH R. HARDIMAN
NASD President and
Member of the Board
Washington, D.C.

(standing left to right)

*JOHN NAISBITT
The Naisbitt Group
Washington, D.C.

THOMAS W. BORDEN
Stone & Youngberg
San Francisco, California

CHARLES E. ZIVNEY
PaineWebber Incorporated
Forth Worth, Texas

PATRICK C. RYAN
Johnston, Lemon & Co.
Incorporated
Washington, D.C.

JOHN G. HIGGINS
Kidder, Peabody & Co.
Incorporated
Boston, Massachusetts
NASD Vice Chairman-Finance, 1987

*WALTER B. GERKEN
Pacific Mutual Life Insurance
Company
Newport Beach, California

JAMES M. DAVIN
The First Boston Corporation
New York, New York
NASD Chairman, 1987

** Governor-at-Large*



To Serve Until January 1989

(seated left to right)

*STEPHEN L. HAMMERMAN
Merrill Lynch & Co., Inc.
New York, New York
NASD Chairman, 1988

RICHARD L. HINTON
Campbell, Waterman Inc.
Seattle, Washington
NASD Vice Chairman, 1988

*THOMAS C. SULLIVAN
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Medina, Ohio

DAVID L. BAKER
Baker & Co., Incorporated
Cleveland, Ohio

(standing left to right)

JOSEPH V. MISSETT, III
Oppenheimer & Co., Inc.
New York, New York

LYNN P. REITNOUER
Crowell, Weedon & Co.
Los Angeles, California

JUDITH G. BELASH
Goldman, Sachs & Co.
New York, New York

*GEORGE PUTNAM
Putnam Group of Funds
Boston, Massachusetts

ALLEN WEINTRAUB
Advest, Inc.
Hartford, Connecticut
NASD Vice Chairman-Finance, 1988

VICTOR ELTING, III
The Chicago Corporation
Chicago, Illinois

**Governor-at-Large*

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To Serve Until January 1990

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Little Rock, Arkansas

WILLIAM R. TIMKEN
Hambrecht & Quist
Incorporated
San Francisco, California

*GRAHAM H. WHITEHEAD
Jaguar plc
Leonia, New Jersey

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Graduate School of Business
Stanford, California

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Johnson, Lane, Space,
Smith & Co., Inc.
Savannah, Georgia

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Limited
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S. G. Warburg & Co., Inc.
New York, New York

HOWARD L. BLUM, JR.
Ladenburg, Thalmann
& Co., Inc.
New York, New York

JAMES F. PECK
Wyoming Financial
Securities, Inc.
Casper, Wyoming

**Governor-at-Large*



To Serve Until January 1991

(seated left to right)

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Thomas Green & Associates
San Diego, California

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Southwest Securities, Inc.
Dallas, Texas

***JOHN E. PEARSON**
Northwestern National Life
Insurance Company
Minneapolis, Minnesota

(standing left to right)

KENNETH J. WESSELS
Wessels, Arnold & Henderson
Minneapolis, Minnesota

PATRICK C. RYAN
Johnston, Lemon & Co.
Incorporated
Washington, D.C.

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Fechtor, Detwiler & Co., Inc.
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Scotts Valley, California

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Ernst & Company
New York, New York

***ROBERT H. MUNDHEIM**
University of Pennsylvania Law
School
Philadelphia, Pennsylvania

**Governor-at-Large*

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Members of the National Committees, who are appointed by the NASD Board of Governors, make recommendations to the Board on their various areas of responsibility. The Executive, Finance & Audit, and National Business Conduct Committees meet before each Board meeting; all other committees meet as necessary. In addition, special or ad hoc committees and task forces are appointed to study current issues as the need arises.

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- *Joseph V. Missett, III
- *Richard C. Romano
- *Wilson C. Wearn
- *Allen Weintraub
- *Joseph R. Hardiman,
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- *Thomas W. Borden
- *James M. Davin
- *Walter B. Gerken
- *Richard L. Hinton
- John B. Levert, Jr.
- *George Putnam
- *Lynn F. Reitnouer
- *Charles F. Zivney
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- *Ronald E. Buesinger
- *David FitzWilliam-Lay
- *Stephen L. Hammerman
- *John G. McDonald
- *B. H. Rutledge Moore
- *James F. Peck
- *Rudolph C. Sander
- *Charles H. Symington, Jr.
- *William L. Tedford, Jr.
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- Norman T. Wilde, Jr.
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- *Thomas W. Borden
- David W. Hunter
- Justin P. Klein
- Alan B. Levenson
- Peter K. Loeb
- John S. Lutz
- Anthony R. Pierno
- *Richard C. Romano
- David L. Sandborg
- *Charles F. Zivney

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- J. Philip Boesel, Jr.
- Edmund J. Cashman, Jr.
- David C. Grove
- Larry D. Hayden
- *John G. Higgins
- John B. Levert, Jr.
- William B. Madden
- Bernard L. Madoff
- Leonard Mayer
- Glenn R. Oxner
- L. C. Petersen
- Alfred J. Rauschman, Sr.
- *Lynn F. Reitnouer
- *Rudolph C. Sander
- Carl P. Sherr
- James C. Stone, III
- *William R. Timken

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MARGIN**

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Chairman
- Richard L. Bove
- *Victor Elting, III
- Robert Ferrentino
- John P. Geelan
- *Richard L. Hinton
- Nelson S. Kibler
- *B. H. Rutledge Moore
- *William R. Timken

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- Peter A. Fischer
- Alex Hammond-Chambers
- Preston B. Heller, Jr.
- B. Lee Karns
- John H. McConnell
- Raymond A. Mueller
- Roy H. Park, Sr.
- Robert D. Ray
- Glen M. Renfrew
- Albert F. Sloan
- Frank Stronach
- *Thomas C. Sullivan
- William R. Thomas
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- *Howard L. Blum, Jr.
- Edmund J. Cashman, Jr.
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- Bruce S. Foerster
- James S. Frazer, III
- William J. Grant, Jr.
- Robert A. Kleinert
- John Kohl
- Alan B. Levenson
- Christopher S. Moore
- G. Peter O'Brien
- Norman Pessin
- John J. Stockbridge
- Sabin C. Streeter

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- J. Philip Boesel, Jr.
- Rosalie Y. Goldberg
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- *James F. Peck
- William W. Stark, Jr.
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BONDING**

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- *Victor Elting, III
- Leonard Mayer
- *James F. Peck
- Herbert A. Sarkisian, Jr.

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Chairman
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- *Judith G. Belash
- Andrew M. Blum
- Mat M. Johnson
- *John Naisbitt
- *Lynn F. Reitnouer
- *Thomas C. Sullivan
- John N. Tognino
- *Wilson C. Wearn
- *Allen Weintraub

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INVESTOR**

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- Terry W. Goodwin
- *Walter B. Gerken
- Raymond Kurtz
- Alexander Lamont
- Robert A. McLaughlin
- Charles L. Melthouse
- James F. Rothenberg
- Dennis G. Sherva
- Binkley C. Shorts

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INSURANCE**

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- *Walter B. Gerken
- *Richard L. Hinton
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Chairman

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- Peter J. DaPuzzo
- *James M. Davin
- Michael Dritzi
- Thomas Giandoreggio
- *David FitzWilliam-Lay
- *Stephen L. Hammerman
- Alex Hammond-Chambers
- *John G. McDonald
- *Joseph V. Missett, III
- *George Putnam
- John N. Tognino
- *Allen Weintraub

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- Tarrant Cutler
- William W. Hewitt, Jr.
- *John G. Higgins
- Graham Holloway
- Charles M. Kiersch
- David S. Lee
- Harry J. Lister
- *B. H. Rutledge Moore
- William T. Morgan
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- Isidore Galante
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- James F. Hageny
- Michael D. Kinsella
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- James C. Stone, III
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- Arnold P. Wolter

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- Theodore Lisec
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Chairman
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- Mark J. Kennedy
- Peter B. Madoff
- G. Dan Marshall
- Leonard Mayer
- John A. Michaels
- Thomas J. Peltier
- Robert F. Schulman
- Ray Skelton
- John N. Tognino

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- Lewis W. Brothers, Jr.
- *Ronald E. Buesinger
- David A. Dworsky
- *Richard L. Hinton
- Larry D. Hayden
- Thomas J. McAllister
- Glenn R. Oxner
- Allan Pessin
- Thomas J. Tagliamonte
- Madeline H. Weinstein

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Chairman
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- Thomas J. Asher
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- *Victor Elting, III
- Larry D. Hayden
- H. Wayne Howell
- James J. McCormack
- *Lynn P. Reitnouer
- John States
- Thomas J. Tagliamonte
- *Charles E. Zivney

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Chairman
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- Conrad Goodkind
- David Lefevre
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- *William R. Timken

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- J. Patrick Campbell
- George Casey
- Ralph J. Costanza
- Peter T. Dartley
- E. E. Geduld
- John C. Giesea
- Charles Neustein
- William R. Rothe
- Norman Shapiro
- *Thomas C. Sullivan
- John N. Tognino

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- Nicola L. Caporale
- John Cirrito
- Anthony T. Geraci
- Benjamin M. O'Callaghan
- *James F. Peck
- Wendie L. Wachtel
- William J. Winter

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- Robert E. Carlson
- Tarrant Cutler
- *Walter B. Gerken
- Cynthia M. Orcutt
- Jerold H. Rosenblum
- Robert G. Sharp

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Chairman
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- Robert C. Brown
- Stanley Lee Burnham
- *James M. Davin
- *John G. Higgins
- Edward J. Mahoney
- *Richard C. Romano
- Glen R. Shipway
- Robert F. Tighie

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Chairman
- Gerald B. Brenzel
- Larry D. Hayden
- J. Stephen Putnam

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Chairman
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- John F. Cogan, Jr.
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- Larry D. Hayden
- Alan B. Levenson
- John B. Levert, Jr.
- *B. H. Rutledge Moore
- J. Stephen Putnam
- *Richard C. Romano
- *William L. Tedford, Jr.
- *Charles E. Zivney

TASK FORCE—LIMIT ORDERS

- Norman T. Wilde, Jr.,
Chairman
- *David L. Baker
- *Ronald E. Buesinger
- Peter J. DaPuzzo
- John T. Johnson
- *Thomas C. Sullivan
- John N. Tognino
- Victor Wright

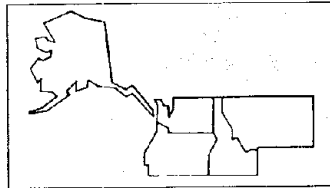
TASK FORCE—REGULATORY REVIEW

- A. A. Sommer, Jr., *Chairman*
- Russell H. Baumgardner
- *Victor Elting, III
- *Stephen L. Hammerman
- Irving M. Pollack
- *Richard C. Romano
- William R. Rothe
- Richard R. West
- *Allen Weintraub

**Member, NASD Board of Governors*

1987 DISTRICT COMMITTEES

Members of the District Committees, who are elected by NASD member firms in their respective areas, supervise NASD programs in the Districts and serve on Business Conduct Committees. In this capacity, they review reports of NASD examiners, investigate complaints against members, conduct disciplinary proceedings, and impose penalties for violations of federal and state laws, Municipal Securities Rulemaking Board rules, and the NASD's Rules of Fair Practice. The Chairmen of the District Committees make up the Advisory Council to the Board of Governors.



DISTRICT 1—Alaska, Idaho, Montana, Oregon, and Washington—180 Members, 1,168 Branches



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Spokane, Washington

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& Smith Incorporated
Seattle, Washington

R. A. Adolphson
Foster & Marshall/
American Express, Inc.
Seattle, Washington

Arthur W. Buerk
Shurgard Securities
Corporation
Seattle, Washington

Kenneth J. Carl
Carl & Company, Incorporated
Portland, Oregon

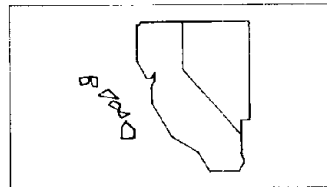
William W. Gallagher
Gallagher Capital Corp.
Portland, Oregon

Larry P. Morris
Dean Witter Reynolds Inc.
Bellevue, Washington

Robert J. Mortell, Jr.
Cable, Howse & Ragen
Seattle, Washington

Eldon J. Wicklund
Smith Barney, Harris Upham
& Co. Incorporated
Eugene, Oregon

Bradford M. Patterson, *Director*
One Union Square, Suite 1911
Seattle, Washington 98101
(206) 624-0790



DISTRICT 2—California, Nevada, and Hawaii—936 Members, 3,254 Branches



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Oakland, California

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Tustin, California

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Christopher Weil & Company,
Inc.
Monterey, California

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Bateman Eichler, Hill Richards,
Incorporated
Sonoma, California

Neil Hennessey
PaineWebber Incorporated
Sacramento, California

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Franklin Distributors, Inc.
San Mateo, California

Carl Lindros
Santa Barbara Securities, Inc.
Santa Barbara, California

John D. Mackey
Henry F. Swift & Co.
San Francisco, California

Anthony W. Martin
Prudential Bache Securities Inc.
Reno, Nevada

Douglas M. McKnight
Dean Witter Reynolds Inc.
La Jolla, California

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Chilton & O'Connor, Inc.
Los Angeles, California

Fredric M. Roberts
F. M. Roberts & Company, Inc.
Los Angeles, California

John J. Sanders
Robertson, Colman & Stephens
San Francisco, California

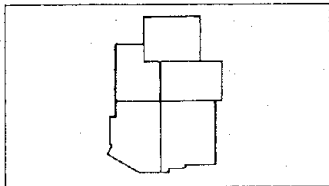
Arnold Seidel
Morton Seidel & Company Inc.
Los Angeles, California

John S. Simmers
Financial Network Investment
Corporation
Torrance, California

Richard E. Waldron
The First Boston Corporation
Los Angeles, California

Kve Hellmers, *Director*
300 South Grand Avenue, 16th
Floor
Los Angeles, California 90071
(213) 627-2122

Theodore F. Schmidt, *Director*
425 California Street, Room
1400
San Francisco, California 94101
(415) 781-3434



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New Mexico, Utah, and
Wyoming—360 Members, 1,374
Branches



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Denver, Colorado

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Reeves and Company,
Investments and
Securities, Inc.
Cheyenne, Wyoming

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Wilson-Davis & Co.
Salt Lake City, Utah

George N. Donnelly
Hanifen, Imhoff Inc.
Denver, Colorado

Stanley R. Fallis
Boettcher & Company, Inc.
Denver, Colorado

Robert A. Fitzner, Jr.
Pitcock Financial Corporation
Englewood, Colorado

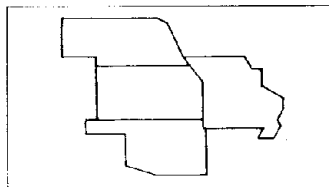
David Nelson
Covey & Company, Inc.
Salt Lake City, Utah

J. Phillip Oelze
Dean Witter Reynolds Inc.
Scottsdale, Arizona

Robert W. Plenge
Plenge, Thomas & Company
Incorporated
Phoenix, Arizona

Forrest D. Smith
Merrill Lynch, Pierce, Fenner
& Smith Incorporated
Albuquerque, New Mexico

Frank J. Birgfeld, *Director*
1401 17th Street, Suite 700
Denver, Colorado 80202
(303) 298-7234



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Nebraska, and Oklahoma—225
Members, 1,166 Branches



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Kansas City, Missouri

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Vice Chairman
Smith Barney, Harris Upham &
Co., Incorporated
Kansas City, Missouri

Jerry P. Oakley, *Vice Chairman*
Sifel, Nicolais & Company, Inc.
Oklahoma City, Oklahoma

Douglas C. Black
B. C. Christopher Securities Co.
Kansas City, Missouri

Lamar S. Jones
Kirkpatrick, Pettis, Smith,
Polian Inc.
Omaha, Nebraska

Rodney O. McWhinney
Waddell & Reed, Inc.
Kansas City, Missouri

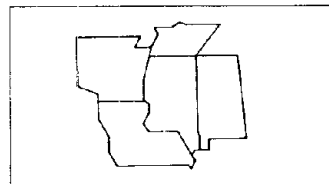
Peter J. O'Neal
I. M. Simon & Co., Inc.
Clayton, Missouri

John M. Phelan
Edward D. Jones & Co.
Maryland Heights, Missouri

Robert L. Schaeffer
The Columbian Securities
Corporation
Topeka, Kansas

Stephen S. Soden
BMA Financial Services, Inc.
Kansas City, Missouri

Jack Rosenfield, *Director*
12 Wyandotte Plaza
120 West 12th Street, Suite 900
Kansas City, Missouri 64105
(816) 421-5700



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Tennessee—227 Members, 824
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Little Rock, Arkansas

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Little Rock, Arkansas

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Sterne, Agee and Leach, Inc.
Birmingham, Alabama

T. Eugene Newton
Howard, Weil, Labouisse,
Friedrichs Incorporated
New Orleans, Louisiana

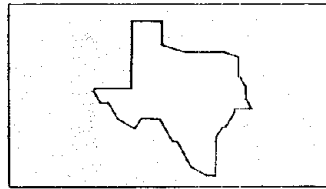
William T. (Dale) Patterson
Geary & Patterson, Incorporated
Jackson, Mississippi

Kenneth P. Toler
A. G. Edwards & Sons, Inc.
Jackson, Mississippi

James L. Vining
Vining-Sparks Securities, Inc.
Memphis, Tennessee

George M. Wood, Jr.
George M. Wood & Company,
Inc.
Montgomery, Alabama

Warren A. Butler, Jr., *Director*
1004 Richards Building
New Orleans, Louisiana 70112
(504) 522-6527



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1,238 Branches**



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Rauscher Pierce Reifsnics, Inc.
San Antonio, Texas

Thomas K. Mercer
ISC Securities, Inc.
Houston, Texas

Vernon Minton
V. E. Minton Securities, Inc.
Forth Worth, Texas

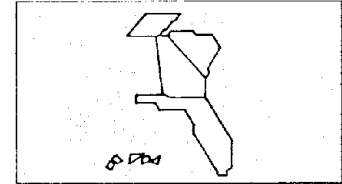
Theodore Mook, Jr.
Tucker, Anthony & R. L. Day, Inc.
Dallas, Texas

Philip E. Nichol
Kidder, Peabody & Co.
Incorporated
Amarillo, Texas

Richard D. Niemann
Shearson Lehman Hutton, Inc.
Corpus Christi, Texas

Tullis C. Thomas, II
Prudential Bache Securities Inc.
San Antonio, Texas

Peter M. Walker, *Director*
1999 Bryan Street, Suite 1450
Olympia & York Tower
Dallas, Texas 75201
(214) 969-7050



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South Carolina, Eastern Tennessee,
Puerto Rico, Canal Zone, and Virgin
Islands—656 Members, 2,776
Branches**



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*Chairman***
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Atlanta, Georgia

Maxwell F. Benson, Jr., *Vice
Chairman*
Jacques Miller Financial Services
Brentwood, Tennessee

Henry T. Blackstock
Investstock & Company, Inc.
Jacksonville Beach, Florida

Robert J. Glenn
The Robinson-Humphrey
Company Inc.
Atlanta, Georgia

John B. Keeble, III
FSC Securities Corporation
Atlanta, Georgia

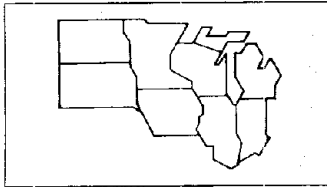
Patrick E. Mann
H. G. Nix, Inc.
Tampa, Florida

Bernard F. Puckhaber
Johnson, Lane, Space, Smith
& Co., Inc.
Charleston, South Carolina

John R. Smith, Jr.
Lowry Financial Services
Corporation
North Palm Beach, Florida

Robert J. Stemmermann
Merrill Lynch, Pierce, Fenner
& Smith Incorporated
Sarasota, Florida

Bennett Whipple, *Vice President,
Director*
One Securities Centre, Suite 500
3490 Piedmont Road, N.E.
Atlanta, Georgia 30305
(404) 239-6100



DISTRICT 8—*Illinois, Indiana,
Iowa, Michigan, Minnesota, North
Dakota, South Dakota, and
Wisconsin*—829 Members, 3,600
Branches



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Minneapolis, Minnesota

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M. B. Vick & Company
Chicago, Illinois

John L. Burbridge
IDS Financial Services, Inc.
Minneapolis, Minnesota

Robert M. Chambers
Stifel, Nicolaus & Company,
Incorporated
Des Moines, Iowa

Richard L. Davis
Kidder, Peabody & Co.
Incorporated
Milwaukee, Wisconsin

Gerald A. Horwitz
Horwitz, Schakner & Associates,
Inc.
Skokie, Illinois

Conrad W. Koski
First of Michigan Corporation
Detroit, Michigan

Richard D. Lauer
Mesirow Brokerage Services, Inc.
Sioux Falls, South Dakota

Peter S. Logan, Sr.
Roney & Co.
Detroit, Michigan

Scott E. Martin
Van Kampen Merritt Inc.
Lisle, Illinois

Thomas J. McAllister
Governors Capital, Inc.
Olympia Fields, Illinois

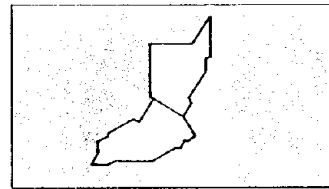
Richard E. Neal
City Securities Corporation
Indianapolis, Indiana

Andrew B. Neely
The Illinois Company
Chicago, Illinois

George H. Shelton
Howe, Barnes & Johnson, Inc.
Chicago, Illinois

John E. Sundeen
Robert W. Baird & Co.
Incorporated
Milwaukee, Wisconsin

E. Craig Dearborn, *Director*
1680 Three First National Plaza
70 West Madison
Chicago, Illinois 60602
(312) 899-4400



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Investment Company
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W. Michael Brady
Dean Witter Reynolds Inc.
Columbus, Ohio

James A. Francis
The Ohio Company
Columbus, Ohio

Michael P. Saracusa
McDonald & Company
Securities, Inc.
Cleveland, Ohio

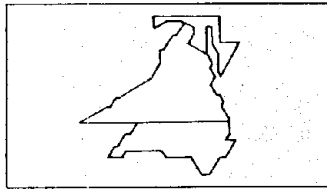
Rudy L. Vincenti
J. C. Bradford & Co.,
Incorporated
Louisville, Kentucky

Margaret M. Wehmeyer
Gradison & Company
Incorporated
Cincinnati, Ohio

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Fifth Floor
Cleveland, Ohio 44114
(216) 694-4545

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Richmond, Virginia

Joseph J. Roberts
Baker, Watts & Co.
Baltimore, Maryland

Norman B. Schrott
A. G. Edwards & Sons, Inc.
Alexandria, Virginia

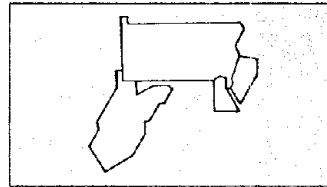
Randall N. Smith
DeRand Investment
Corporation of America
Arlington, Virginia

Frank H. Stringfellow
Jefferson-Pilot Investor Services,
Inc.
Greensboro, North Carolina

Ben T. Vernon
Dean Witter Reynolds Inc.
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Donald P. Whitley
PaineWebber Incorporated
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Butcher & Singer Inc.
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Hopper Soliday & Co., Inc.
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Merrill Lynch, Pierce, Fenner
& Smith Incorporated
Morristown, New Jersey

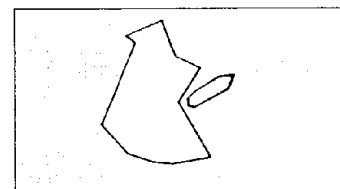
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F. J. Morrissey & Co. Inc.
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Richard M. O'Brien
Parker/Hunter Incorporated
Pittsburgh, Pennsylvania

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Janney Montgomery Scott Inc.
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19103
(215) 665-1180



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Company of New York
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Alfred Reeves
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Corporation of America
New York, New York

Robert A. Spira
Haas Securities Corporation
New York, New York

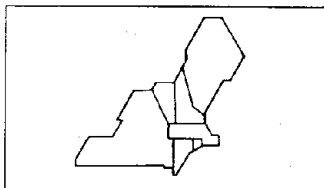
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Cazenove Incorporated
New York, New York

Leopold Swergold
Swergold, Chefitz &
Sinsabaugh Inc.
New York, New York

John N. Tognino
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& Smith Incorporated
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Bruce Tullo
Merrill Lynch, Pierce, Fenner
& Smith Incorporated
New York, New York

William S. Clendenin,
Vice President, Director
NASD Financial Center
33 Whitehall Street
New York, New York 10004
(212) 858-4000



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M. Griffith, Inc.
Utica, New York

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Cynthia M. Orcutt
Sun Investment Services
Company
Wellesley Hills, Massachusetts

Gerald H. Powers
Cantella & Co. Inc.
Boston, Massachusetts

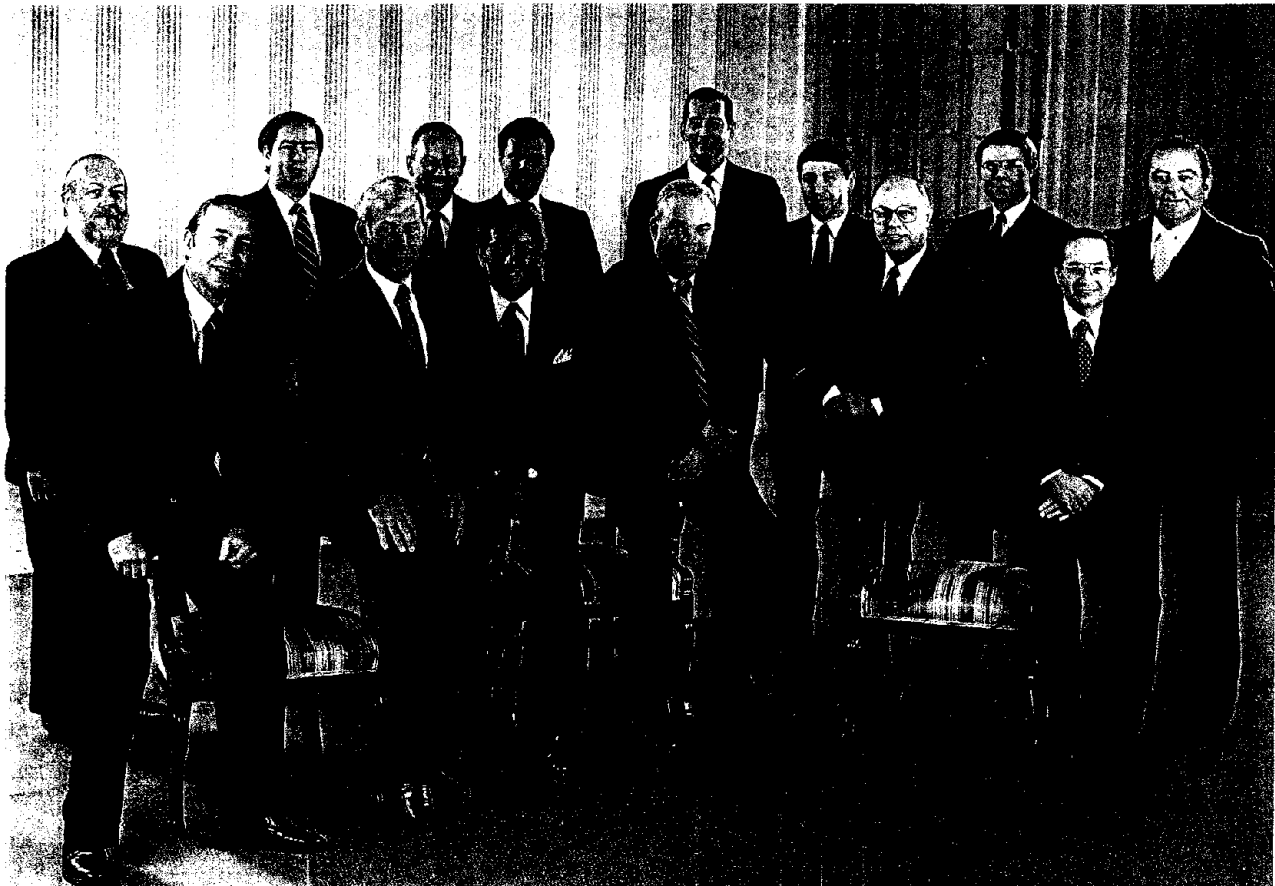
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Trubee Collins and Co.
Buffalo, New York

Lewis J. Sperber
Sperber, Adams & Co.
Westport, Connecticut

Robert D. Watral
Quick & Reilly, Inc.
Boston, Massachusetts

Willis H. Riccio,
Vice President, Director
260 Franklin Street, 20th Floor
Boston, Massachusetts 02110
(617) 439-4404

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(standing left to right)

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Director, District 5
New Orleans, Louisiana

Peter M. Walker
Director, District 6
Dallas, Texas

Kye Hellmers
Director, District 2S
Los Angeles, California

Bradford M. Patterson
Director, District 1
Seattle, Washington

William H. Jackson, Jr.
Director, District 9
Cleveland, Ohio

John P. Nocella
Director, District 11
Philadelphia, Pennsylvania

Theodore F. Schmidt
Director, District 2N
San Francisco, California

(seated left to right)

Frank J. Birgfeld
Director, District 3
Denver, Colorado

Thomas P. Forde
Director, District 10
Washington, D.C.

Willis H. Riccio
Vice President, Director
District 13
Boston, Massachusetts

William S. Clendenin
Vice President, Director
District 12
New York, New York

Bennett Whipple
Vice President, Director
District 7
Atlanta, Georgia

Jack Rosenfield
Director, District 4
Kansas City, Missouri

CONSOLIDATED BALANCE SHEETS

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

<i>September 30 (in thousands)</i>	1987	1986
ASSETS		
Current Assets		
Cash	\$ 1,376	\$ 1,313
Investments, principally U.S. government securities, at cost (approximate market value of \$83,908 in 1987 and \$88,190 in 1986)	85,278	86,799
Receivables and other current assets	8,985	8,286
Total current assets	95,639	96,398
Property and equipment		
Land, buildings, and improvements	29,608	16,372
Data processing, subscriber equipment, and software	56,533	45,197
Furniture, equipment, and leasehold improvements	15,467	11,122
	101,608	72,691
Less accumulated depreciation and amortization	35,860	33,788
	65,748	38,903
Other assets	3,640	2,944
	\$165,027	\$138,245
LIABILITIES AND EQUITY		
Current liabilities		
Accounts payable and accrued expenses	\$ 15,981	\$ 12,344
Deferred income and deposits	11,013	10,010
Current portion of obligations under capital leases	1,818	1,294
Note payable		200
Total current liabilities	28,812	23,848
Obligations under capital leases	5,912	1,142
Other liabilities	4,281	3,049
Total liabilities	39,005	28,039
Equity	126,022	110,206
	\$165,027	\$138,245

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME AND EQUITY

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

<i>Year Ended September 30 (in thousands)</i>	1987	1986
INCOME		
Market information service fees	\$ 52,854	\$ 43,207
Registration and examination fees	30,801	25,366
Member assessments	25,702	21,800
Interest and other	15,068	16,157
NASDAQ issuers fees	13,283	10,633
Corporate finance fees	7,069	7,338
	144,777	124,501
EXPENSES		
Salaries and employee benefits	63,763	49,499
Professional and other services	14,412	11,429
Equipment maintenance and data transmission	12,910	10,290
Depreciation and amortization	10,363	7,376
Office expense	10,052	8,015
Publications, supplies, and postage	6,196	5,250
Travel and meetings	6,028	4,860
Other	2,172	1,213
	125,896	97,932
Income before provision for income taxes	18,881	26,569
Provision for income taxes	3,065	2,897
Net income	15,816	23,672
Equity at beginning of year	110,206	86,534
Equity at end of year	\$126,022	\$110,206

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

<i>Year Ended September 30 (in thousands)</i>	1987	1986
FINANCIAL RESOURCES WERE PROVIDED BY:		
Net income	\$15,816	\$23,672
Add items not affecting working capital:		
Depreciation and amortization	10,363	7,376
Other	935	
WORKING CAPITAL PROVIDED BY OPERATIONS	27,114	31,048
Increase in obligations under capital leases	6,991	411
Increase in other liabilities	1,232	1,675
	35,337	33,134
FINANCIAL RESOURCES WERE USED FOR:		
Additions to property and equipment	39,018	18,244
Decrease in long-term obligations under capital leases	1,346	1,294
Increase in other assets	696	409
	41,060	19,947
INCREASE (DECREASE) IN WORKING CAPITAL	\$ (5,723)	\$ 13,187
ANALYSIS OF CHANGES IN WORKING CAPITAL		
Increase (decrease) in current assets:		
Cash	\$ 63	\$ 250
Investments	(1,521)	16,279
Receivables and other current assets	699	1,751
	(759)	18,280
Increase (decrease) in current liabilities:		
Accounts payable and accrued expenses	3,637	2,935
Deferred income and deposits	1,003	3,689
Current portion of obligations under capital leases	524	(131)
Note payable	(200)	(1,400)
	4,964	5,093
INCREASE (DECREASE) IN WORKING CAPITAL	\$ (5,723)	\$ 13,187

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Business Segments:

The consolidated financial statements include the accounts of the National Association of Securities Dealers, Inc. (NASD), and its wholly owned subsidiaries, including NASDAQ, Inc., and NASD Market Services, Inc. (MSI), after elimination of all significant intercompany transactions. The consolidated financial statements have been prepared on the accrual basis of accounting and conform to generally accepted accounting principles.

NASD is a membership association established to regulate the over-the-counter securities market. NASDAQ, Inc., owns and operates the international, electronic NASDAQ quote information system. MSI provides national market facilities to assist the NASD in carrying out its regulatory responsibilities and for the benefit of NASD members in their pursuit of efficient execution of securities transactions.

Property and Equipment, Depreciation and Amortization:

Property and equipment are recorded at cost. Equipment acquired under capital leases is recorded at the lower of fair market value or the present value of future lease payments. Depreciation and amortization are provided on the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the period of the applicable lease.

Software Costs:

Purchased software, developed by others, is capitalized if it has a continuing value and is considered an integral part of purchased hardware. All other software development costs are charged to expense as incurred.

Pension:

Pension expense includes charges for current service and amortization of prior service costs over an average of 30 years. The NASD funds pension costs in accordance with the funding provisions of the Employee Retirement Income Security Act.

Income Taxes:

NASD and NASDAQ, Inc., are tax-exempt, not-for-profit organizations. MSI is a taxable entity and recognizes cer-

tain expenses, principally start-up expenditures and depreciation, in different periods for income tax purposes than for financial reporting purposes.

Reclassification:

Certain 1986 amounts have been reclassified for comparative purposes.

NOTE B—BUSINESS SEGMENTS

<i>(in thousands)</i>	<i>NASD</i>	<i>NASDAQ</i>	<i>MSI</i>	<i>Consolidated</i>
1987				
Income	\$ 90,364	\$ 37,392	\$ 17,115	\$ 144,777
Expenses, including income taxes	82,318	32,736	14,001	128,961
Net income	\$ 8,046	\$ 4,656	\$ 3,114	\$ 15,816
Total assets	\$ 110,187	\$ 45,906	\$ 9,717	\$ 165,027
Equity	84,265	34,691	8,217	126,022
1986				
Income	\$ 78,151	\$ 31,919	\$ 14,665	\$ 124,501
Expenses, including income taxes	65,581	24,392	11,090	100,829
Net income	\$ 12,570	\$ 7,527	\$ 3,575	\$ 23,672
Total assets	\$ 96,571	\$ 34,851	\$ 7,564	\$ 138,245
Equity	76,219	30,035	5,103	110,206

Intercompany billings, payables, and receivables have been eliminated from the consolidated financial data.

NOTE C—LEASES

Data processing, subscriber equipment, and software include the following amounts relating to leases which have been capitalized. The initial terms of the capitalized leases are 36 to 60 months.

<i>September 30 (in thousands)</i>	1987	1986
Data processing equipment	\$9,620	\$8,372
Less accumulated depreciation	1,769	5,951
	\$7,851	\$2,421

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

NASD leases certain office space and equipment in connection with its operations. The majority of these leases contain escalation clauses based on increases in property taxes and building operating costs. Certain of these leases also contain renewal options. No lease extends beyond 1997. Future minimum lease payments under the capital leases and noncancelable operating leases with initial or remaining terms of one year or more consisted of the following at September 30, 1987 (in thousands):

<i>Fiscal Year Ending September 30</i>	<i>Capital Leases</i>	<i>Operating Leases</i>
1988	\$2,319	\$ 3,529
1989	2,033	3,947
1990	1,817	3,989
1991	1,590	3,994
1992	1,126	3,624
Remaining years		10,092
Total minimum lease payments	8,885	29,175
Less: Amount representing interest	1,155	
Present value of net minimum lease payments	7,730	
Less: Amounts due in one year	1,818	
	\$5,912	\$29,175

Rent expense for operating leases was \$3,695,000 in 1987 and \$3,087,000 in 1986.

On October 30, 1987, the NASD entered into a 15-year lease agreement for additional office space. Lease payments, net of sublease income, will be approximately \$1,333,000 annually.

NOTE D—RETIREMENT BENEFITS

NASD maintains a non-contributory defined benefit pension plan for the benefit of all eligible employees. Pension expense for the years 1987 and 1986 aggregated \$2,625,000 and \$2,637,000, respectively. Pension costs have been determined in accordance with Accounting

Principles Board Opinion Number 8. A comparison of accumulated pension plan benefits and net pension plan assets as of the most recent valuation dates is presented below:

<i>January 1 (in thousands)</i>	1987	1986
Actuarial present value of accumulated plan benefits:		
Vested	\$ 7,449	\$ 7,235
Nonvested	3,043	1,721
	\$10,492	\$ 8,956
Net assets available for plan benefits	\$20,001	\$15,999

The average assumed rate of return used in determining the actuarial present value of accumulated plan benefits was 7 percent for 1987 and 1986. NASD also maintains two savings plans for employees. Eligibility for both plans is based upon length of service. Participation in the plans is voluntary. Savings plan expense for the years 1987 and 1986 was \$786,000 and \$699,000, respectively.

NOTE E—INCOME TAXES

The income tax provision for the years ended September 30, 1987 and 1986 consisted of the following:

<i>(in thousands)</i>	1987	1986
Current expense		
Federal	\$2,275	\$2,015
State	616	540
Deferred expense	174	342
	\$3,065	\$2,897

The tax provision was reduced by investment tax credit utilization of \$429,000 in 1986.

NOTE F—CONTINGENCIES

There are legal proceedings pending against the NASD, separately or with others. Management believes, based upon the opinion of counsel, that liabilities arising from these proceedings, if any, will not have a material effect on the NASD.

REPORT OF INDEPENDENT ACCOUNTANTS

REPORT OF INDEPENDENT ACCOUNTANTS

Board of Governors
National Association of
Securities Dealers, Inc.
Washington, D.C.

We have examined the consolidated balance sheets of the National Association of Securities Dealers, Inc., and subsidiaries as of September 30, 1987 and 1986, and the related consolidated statements of income and equity, and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the consolidated financial position of the National Association of Securities Dealers, Inc., and subsidiaries as of September 30, 1987 and 1986, and the consolidated results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Ernst & Whinney

Washington, D.C.
December 18, 1987

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President, NASD

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President, NASD

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Administrative Services*
- Bennett Whipple, *Vice President
District Director*
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NASD

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