

SECURITIES AND EXCHANGE COMMISSION
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OPENING STATEMENT OF
THE HONORABLE HAROLD M. WILLIAMS, CHAIRMAN
SECURITIES AND EXCHANGE COMMISSION

AT THE

OCCASION OF THE COMMISSION'S CONSIDERATION
OF RULE 19C-3, PROPOSED
IN SECURITIES EXCHANGE ACT RELEASE NO. 15769

THE COMMISSION, THIS MORNING, IS CONSIDERING WHETHER TO ADOPT PROPOSED
RULE 19C-3 UNDER THE SECURITIES EXCHANGE ACT, WHICH WOULD AMEND EXISTING
RULES OF THE VARIOUS NATIONAL SECURITIES EXCHANGES LIMITING OFF-BOARD
TRANSACTIONS BY THEIR MEMBERS AND CURRENTLY PROHIBITING MOST FIRMS FROM
MAKING MARKETS OVER-THE-COUNTER IN LISTED SECURITIES. RULE 19C-3, IF ADOPTED,
WOULD PRECLUDE THE APPLICATION OF EXCHANGE OFF-BOARD TRADING RESTRICTIONS TO
CERTAIN EQUITY SECURITIES WHICH WERE NOT EXCHANGE TRADED ON APRIL 26, 1979, OR
WHICH WERE EXCHANGE TRADED ON THAT DATE, BUT WHICH FAIL TO REMAIN
CONTINUOUSLY EXCHANGE TRADED THEREAFTER.

EXCHANGE RULES WHICH IMPOSE RESTRICTIONS ON OFF-BOARD TRADING BY
EXCHANGE MEMBERS HAVE BEEN THE SUBJECT OF TWO PRIOR REGULATORY PROCEEDINGS
INSTITUTED BY THE COMMISSION. THE FIRST OF THESE PROCEEDINGS, WHICH BEGAN
SHORTLY AFTER THE ADOPTION OF THE 1975 AMENDMENTS TO THE EXCHANGE ACT,
CULMINATED IN THE ADOPTION OF RULE 19C-1 UNDER THE ACT, ELIMINATING OFF-BOARD
TRADING RESTRICTIONS WITH RESPECT TO AGENCY TRANSACTIONS BY MEMBERS OF
EXCHANGES (EXCEPT FOR SO-CALLED "IN-HOUSE" CROSSES). THE SECOND PROCEEDING

HAS PRIMARILY FOCUSED ON PROPOSED RULE 19C-2, WHICH, IF ADOPTED, WOULD REMOVE ALL OFF-BOARD TRADING RESTRICTIONS ON PRINCIPAL TRANSACTIONS AND "IN-HOUSE" AGENCY CROSSES WITH RESPECT TO ALL REPORTED SECURITIES. TO DATE, THE COMMISSION HAS NOT TAKEN ANY FINAL ACTION ON PROPOSED RULE 19C-2.

ON APRIL 26, 1979, THE COMMISSION ISSUED A RELEASE ANNOUNCING THE INSTANT PROCEEDING, INCLUDING PUBLIC HEARINGS, TO CONSIDER RULEMAKING TO AMEND OFF-BOARD TRADING RESTRICTIONS WITH RESPECT TO A MORE LIMITED GROUP OF SECURITIES -- NEWLY LISTED SECURITIES. IN ADDITION TO RECEIVING WRITTEN COMMENT, THE COMMISSION HELD SIX DAYS OF ORAL HEARINGS, BEGINNING ON JUNE 20, 1979, AND CONCLUDING ON JULY 2, 1979. THE NUMBER OF, AND DIVERSITY OF OPINION EVIDENCED BY, THE COMMENTS RECEIVED BY THE COMMISSION REFLECTS THE IMPORTANCE AND DIFFICULTY OF THE ISSUES RAISED BY PROPOSED RULE 19C-3. I WOULD ALSO POINT OUT THAT, IN CONSIDERING THIS PROPOSAL, THE COMMISSION HAD BEFORE IT THE RECORD AND TRANSCRIPTS OF THE TWO PRIOR PROCEEDINGS AND INCORPORATED THAT MATERIAL BY REFERENCE INTO THE RECORD OF THE CURRENT PROCEEDING.

THE COMMISSION FOUND IN ITS EARLIER PROCEEDINGS THAT OFF-BOARD TRADING RESTRICTIONS HAVE ANTICOMPETITIVE EFFECTS, IN THAT THEY EFFECTIVELY CONFINE TRADING IN LISTED SECURITIES TO EXCHANGE MARKETS BY PRECLUDING EXCHANGE MEMBERS FROM TRADING AS PRINCIPALS IN THE OVER-THE-COUNTER MARKET. THAT CONCLUSION, HOWEVER, DOES NOT, AS A LEGAL MATTER, END THE INQUIRY. TO THE CONTRARY, THE EXCHANGE ACT REQUIRES THE COMMISSION TO BALANCE THE NEED TO REMOVE ANTICOMPETITIVE ASPECTS OF THESE TYPES OF EXCHANGE RULES AGAINST ANY PURPOSES OF THE ACT WHICH ARE SERVED BY THEIR CONTINUED APPLICATION. IN OTHER WORDS, THE COMMISSION MUST DETERMINE WHETHER THE POTENTIAL BENEFITS TO BE ACHIEVED BY ADOPTION OF THIS LIMITED PROPOSAL ARE OUTWEIGHED BY THE POSSIBILITY OF ADVERSE CONSEQUENCES.

IN MAKING A DETERMINATION OF THIS KIND, THE COMMISSION MUST CONSIDER CONCERNS RAISED BY VARIOUS COMMENTATORS -- MOST NOTABLY, THAT ADOPTION OF THE PROPOSAL, EVEN THOUGH IT WOULD CURRENTLY IMPACT ONLY A SMALL NUMBER OF STOCKS, WOULD PERMIT A SIGNIFICANT AMOUNT OF INTERNALIZED TRADING BY BROKER-DEALER FIRMS WITH LARGE RETAIL ORDER FLOW OR SIZEABLE CORRESPONDENT NETWORKS

WHICH, IN TURN, WOULD HAVE SIGNIFICANT ADVERSE EFFECTS ON THE MARKETS FOR THOSE SECURITIES. AGAINST THESE CONCERNS, THE COMMISSION MUST WEIGH THE POSSIBILITY THAT THE RULE MIGHT RESULT IN INCREASED MARKET MAKER COMPETITION AND SHOULD PROVIDE A USEFUL LEARNING EXPERIENCE TO THE COMMISSION AND THE SECURITIES INDUSTRY IN A NUMBER OF AREAS. MOST IMPORTANTLY, WHILE THE RULE, IF ADOPTED, WILL NOT YIELD EMPIRICAL DATA SUFFICIENT TO SUPPORT DEFINITIVE CONCLUSIONS REGARDING THE REMOVAL OF REMAINING OFF-BOARD TRADING RESTRICTIONS, ADOPTION OF THE RULE SHOULD NEVERTHELESS PROVIDE AN OPPORTUNITY TO STUDY AN ENVIRONMENT CHARACTERIZED BY CONCURRENT OVER-THE-COUNTER AND EXCHANGE TRADING.

BALANCING THE VARIOUS COMPLEX ISSUES ASSOCIATED WITH OFF-BOARD TRADING RULES GENERALLY, AND WITH RULE 19C-3 IN PARTICULAR, IS EXTREMELY DIFFICULT -- IN PART BECAUSE OF THE MULTITUDE OF RELATED ISSUES, AND IN PART BECAUSE OF OUR INABILITY TO RESPOND TO ALL OF THESE ISSUES WITH CERTITUDE AT THIS TIME.

NOTWITHSTANDING THE DELICATE NATURE OF THIS BALANCE, I BELIEVE THAT, AFTER

CONSIDERING AND WEIGHING ALL OF THE FACTORS, THE COMMISSION SHOULD ADOPT THE
RULE.

FIRST, WE MUST REMEMBER THAT THE PROPOSAL IS A LIMITED ONE; IN THE BETTER
THAN 13 MONTHS SINCE THE COMMISSION ANNOUNCED THE RULE 19C-3 PROCEEDING, JUST
OVER 60 SECURITIES BECAME NEWLY-LISTED AND, THUS, SUBJECT TO THE RULE. SECOND,
THE STAFF OF THE COMMISSION HAS DEVELOPED A COMPREHENSIVE MONITORING
PROGRAM WHICH IT WILL IMPLEMENT IF RULE 19C-3 IS ADOPTED. THIS MONITORING
PROGRAM, ALONG WITH ADDITIONAL INPUT FROM INTERESTED PARTIES, SHOULD ENABLE
THE COMMISSION TO IDENTIFY ANY ADVERSE EFFECTS ON THE SECURITIES MARKETS
RESULTING FROM THE REMOVAL OF OFF-BOARD TRADING RESTRICTIONS FOR 19C-3
SECURITIES AND TO REACT QUICKLY BY ADOPTING ONE OF THE OUTSTANDING
OVERREACHING RULES, ENGAGING IN FURTHER PROPHYLACTIC RULEMAKING, OR, IF
NECESSARY, RESCINDING THE RULE ITSELF. MORE GENERALLY, THE STAFF HAS INDICATED
THAT THE MONITORING PROGRAM WILL PROVIDE THE COMMISSION WITH SUFFICIENT
INFORMATION TO PERMIT IT TO MAKE ANNUAL PUBLIC REPORTS ON THE EFFECTS OF THE
RULE, TO HOLD ANNUAL PUBLIC MEETINGS TO DISCUSS WITH INTERESTED PARTIES THE

YEAR'S EXPERIENCE UNDER THE RULE, AND TO REVISIT THE QUESTION OF OFF-BOARD TRADING RESTRICTIONS GENERALLY AT AN APPROPRIATE FUTURE TIME.

PENDING SUCH A GENERAL REVIEW, I BELIEVE THAT THE COMMISSION SHOULD TODAY ALSO GIVE SERIOUS CONSIDERATION TO THE WITHDRAWAL OF PROPOSED RULE 19C-2. IN LIGHT OF RULE 19C-3, IT APPEARS UNLIKELY THAT THE COMMISSION WILL FIND IT APPROPRIATE IN THE VERY NEAR FUTURE TO TAKE ANY FURTHER ACTION TO ELIMINATE OFF-BOARD TRADING RESTRICTIONS GENERALLY. MOREOVER, I BELIEVE THAT, IN LIGHT OF THE AMOUNT OF TIME WHICH HAS ELAPSED SINCE RULE 19C-2 WAS ORIGINALLY PROPOSED, ANY RECONSIDERATION OF THAT RULE SHOULD BE, IN EFFECT, DE NOVO, BASED ON A COMPLETE CONSIDERATION OF DEVELOPMENTS IN THE MARKETS TO THAT DATE, AND ACCOMPANIED BY THE FULL PROCEDURAL REQUIREMENTS OF SECTION 19(C) OF THE ACT, INCLUDING ANOTHER SERIES OF ORAL HEARINGS. IN ADDITION, THE OVERHANG OF A RULE PROCEEDING AS PERVASIVE AS THAT INVOLVED IN PROPOSED RULE 19C-2 HAS, ON OCCASION, RAISED CONCERNS REGARDING EX PARTE CONTACTS UNDER THE ADMINISTRATIVE PROCEDURE ACT; SUCH A CONSIDERATION SHOULD NOT BE ALLOWED TO INTERFERE WITH THE MUCH-NEEDED ABILITY AND WILLINGNESS OF THE COMMISSION AND

ALL INTERESTED PARTIES TO ENGAGE IN A CONSTRUCTIVE DIALOGUE AND TO WORK TOGETHER TOWARDS A RESOLUTION OF THE MANY IMPORTANT ISSUES LEADING TO IMPLEMENTATION OF A NATIONAL MARKET SYSTEM. ACCORDINGLY, I WOULD PERSONALLY FAVOR FORMALLY WITHDRAWING PROPOSED RULE 19C-2 AT THIS TIME.

EVEN WITHIN THE LIMITED CONTEXT OF RULE 19C-3, HOWEVER, THE REMOVAL OF OFF-BOARD TRADING RESTRICTIONS RAISES A NUMBER OF COMPLEX POLICY ISSUES RELATING TO THE CURRENT MARKET STRUCTURE. ON THE ONE HAND, REMOVAL OF THESE RESTRICTIONS MAY BE THE MOST EFFECTIVE TOOL WHICH THE COMMISSION POSSESSES TO MEET ITS STATUTORY DIRECTIVES TO INCREASE COMPETITION IN THE SECURITIES MARKETS AND TO FACILITATE THE DEVELOPMENT OF A NATIONAL MARKET SYSTEM. ON THE OTHER HAND, HOWEVER, THEIR REMOVAL ALSO RAISES SERIOUS CONCERNS REGARDING EQUAL REGULATION AND, MOST IMPORTANTLY, THE EFFECTS OF INCREASED INTERNALIZATION (SUCH AS INCREASED MARKET FRAGMENTATION AND AN ENHANCED POTENTIAL FOR OVERREACHING). AS IN MOST IMPORTANT CHANGES, NO ONE CAN PREDICT WITH CONFIDENCE THE FULL EFFECTS OF REMOVING OFF-BOARD TRADING RESTRICTIONS. HOWEVER, THE LIMITED NATURE OF THE PROPOSAL AND THE COMMISSION'S COMMITMENT

TO A COMPREHENSIVE MONITORING EFFORT SHOULD MINIMIZE POTENTIAL ADVERSE EFFECTS AND MAXIMIZE THE LEARNING POTENTIAL OF THIS EXPERIMENT.

I SHOULD EMPHASIZE, HOWEVER, THAT THE ADOPTION OF RULE 19C-3 DOES NOT REDUCE, AND IN MANY CASES CLEARLY INCREASES, THE IMPORTANCE OF PROMPTLY ACHIEVING A NUMBER OF NATIONAL MARKET SYSTEM GOALS AND INITIATIVES WHICH THE COMMISSION AND THE INDUSTRY HAVE IDENTIFIED. IN THAT CONNECTION, THE NASD'S COMMITMENT TO UPGRADE AND ENHANCE ITS NASDAQ SYSTEM TO PROVIDE A MORE EFFICIENT MECHANISM FOR OVER-THE-COUNTER MARKET MAKING IN LISTED SECURITIES IS A PARTICULARLY IMPORTANT FACTOR IN THE COMMISSION'S DETERMINATION WHETHER TO ADOPT RULE 19C-3. ACCORDINGLY, I WOULD EXPECT THAT THE NASD WILL IMPLEMENT THESE ENHANCEMENTS IN THE NEAR TERM AND CONTINUE TO IMPROVE ITS SYSTEM IN THE FUTURE.

SIMILARLY, THE ADOPTION OF RULE 19C-3 WOULD INCREASE THE NEED TO ACHIEVE EFFECTIVE LINKAGES BETWEEN TRADITIONAL EXCHANGE TRADING FLOORS AND MARKETS CONDUCTED EITHER OVER-THE-COUNTER OR THROUGH ELECTRONIC TRADING SYSTEMS, AND THE COMMISSION FULLY EXPECTS THAT THE NASD AND THE ITS

PARTICIPANTS WILL PROMPTLY CONCLUDE THEIR NEGOTIATIONS AND BEGIN WORK ON CONSUMMATING AN AUTOMATED LINKAGE BETWEEN THE ENHANCED NASDAQ SYSTEM AND THE ITS. THE COMMISSION LIKewise EXPECTS THAT THE CSE AND ITS PARTICIPANTS WILL IMPLEMENT A LINKAGE BETWEEN THEIR SYSTEMS IN THE NEAR FUTURE.

AT THE SAME TIME, THE NASD'S COMMITMENT TO IMPLEMENT A COMPLETE AND THOROUGH SURVEILLANCE PROGRAM WHICH WILL PERMIT THEM TO IDENTIFY CASES OF OVERREACHING BY OVER-THE-COUNTER MARKET MAKERS IS VITAL TO THE OPERATION AND SUCCESS OF RULE 19C-3. DILIGENT SURVEILLANCE BY THE NASD, IN CONJUNCTION WITH THE COMMISSION'S OWN MONITORING EFFORTS, SHOULD WORK TO INCREASE INVESTOR CONFIDENCE IN THE FAIRNESS OF THE OVER-THE-COUNTER MARKETS IN LISTED SECURITIES AND SERVE TO MAKE THE 19C-3 EXPERIENCE A MEANINGFUL ONE.

FINALLY, THE ADOPTION OF THE RULE ALSO INCREASES THE IMPORTANCE OF EARLY ACHIEVEMENT OF OTHER NEAR-TERM GOALS OF THE NATIONAL MARKET SYSTEM, SUCH AS NATIONWIDE PRICE PROTECTION FOR PUBLIC LIMIT ORDERS. THE LOIS INITIATIVE CANNOT BE ALLOWED TO FALTER, AND THE COMMISSION STANDS READY TO REVISIT THE QUESTION WITH A VIEW TOWARDS FURTHER REGULATORY ACTION SHOULD SUCH A COURSE PROVE

NECESSARY OR APPROPRIATE. SIMILARLY, ESPECIALLY IN LIGHT OF THE INCREASED MARKET MAKING COMPETITION WHICH SHOULD RESULT FROM THE ADOPTION OF RULE 19C-3 AND THE CREATION OF A LINKAGE BETWEEN ITS AND THE ENHANCED NASDAQ SYSTEM, THE ITS PARTICIPANTS SHOULD INCREASE THEIR EFFORTS TO REDUCE TO A MINIMUM THE OCCURRENCE OF TRADE-THROUGHS AND DELAYS IN ITS. BY THE SAME TOKEN, FULL COMPLIANCE WITH THE COMMISSION'S FIRM QUOTE RULE BY ALL MARKET CENTERS WILL TAKE ON EVEN MORE SIGNIFICANCE.

IN MY VIEW, THE PROMPT ACHIEVEMENT OF THESE GOALS, AND OTHERS, IS ESSENTIAL TO ENABLE THE COMMISSION AND THE INDUSTRY TO MOVE RESPONSIBLY IN ADVANCING THE PROCESS OF DEVELOPING A NATIONAL MARKET SYSTEM AS REQUIRED BY THE EXCHANGE ACT AMENDMENTS OF 1975.