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Memo to: Steven B. Harris
Counsel
Subcommittee on Securities
Committee on Banking, Housing and Urban Affairs
United States Senate

From: Leigh Snell
David Vienna & Associates

Re: Multiple Trading of Options

Date: June 20, 1988

It was a pleasure to meet with you again recently when Mr. Dale Carlson, Vice President for Government Relations of the Pacific Stock Exchange (PSE), one of my firm's clients, met briefly with Senator Riegle. As you will recall, one of the issues of concern to the PSE is the proposal of the Securities & Exchange Commission for the multiple trading of options.

As promised, enclosed you will find an abbreviated briefing booklet on this issue for your further information. Should you desire even more detail, I have an annotated outline of the four basic arguments in opposition to the proposal which I would be happy to get over to you.

To briefly recap our conversation with Senator Riegle, the Pacific Stock Exchange believes that the Commission is ducking the difficult issues that have been raised by both the Senate Banking Committee as well as the House Energy & Commerce Committee. Their latest "response" in this area does nothing to disabuse us of that notion. Furthermore, given their continued refusal to consider tabling the matter, we are very concerned that the Commission may now believe that the way has been cleared for them to proceed with the adoption of this proposal.

The abbreviated schedule of the Congress for the remainder of this election year makes it increasingly impossible for either the House or the Senate to consider mounting an effective legislative response to the Commission the later into the Fall any action on their part comes. Furthermore, in all likelihood it will not be until early Spring of 1989 before the new Congress is organized enough to be able to pursue a remedy should the SEC take adverse action following adjournment of the 100th Congress this October.

Therefore, as we explained to Senator Riegle, we will be actively pursuing a "moratorium" amendment in the House. This amendment would force the SEC to table its multiple trading proposal for a set period of time; the exact length of time could be pegged to either the Commission's formal evaluation of the issues raised in Congressional correspondence on the subject, or to the completion and review of an Office of Technology Assessment (OTA) study, requested by the House Government Operations Committee, that will be looking at the technological capabilities of the securities industry.

I hope that this material is of some help to you. If you have any further questions, please feel free to give me a call in Alexandria, Virginia, at 684-5236.

Securities Underwriting Applications Approved by or
Pending Before the Board

On April 30, 1987, the Board approved applications by Citicorp, J.P. Morgan and Bankers Trust to underwrite and deal in, to a limited extent, commercial paper, municipal revenue bonds and mortgage-related securities. On July 14, 1987, the Board approved underwriting and dealing in consumer-receivable-related securities.

The Board determined that the bank holding companies would not be "engaged principally" in activities covered by section 20 of the Glass-Steagall Act if they limited their underwriting and dealing revenues from these ineligible securities activities to no more than 5 percent of the gross revenues of the underwriting subsidiaries. Section 20 prohibits a member bank affiliate from being "engaged principally" in underwriting securities.

In its Order, the Board established a framework of conditions to assure that the underwriting activity would be conducted consistent with safe and sound banking practices and avoid conflicts of interest and other adverse effects. These "firewalls," many of which were incorporated in the Proxmire Financial Modernization Act (S. 1886), include restrictions on capital adequacy and extensions of credit by banks to their securities affiliates or to enhance the marketability of securities underwritten by the affiliate. They also require a separation of the securities affiliate from its banking affiliates.

The Securities Industry Association ("SIA") challenged the decision in the U.S. Court of Appeals in New York. The SIA contended that the underwriting subsidiaries were engaged principally in underwriting securities in violation of section 20. On February 8, 1988, the court upheld the Board's position that the underwriting subsidiaries would not be engaged principally in underwriting activities under the 5 percent revenue limitation and that the activity was closely related to banking under the Bank Holding Company Act.

On June 13, the Supreme Court denied the SIA's request to review that decision. This permitted bank holding companies to commence the ineligible underwriting operations.

Since April 30, 1987, the Board has approved applications by 13 additional bank holding companies subject to the 5 percent cap and the firewalls established in its original approval. (Attached is a list of these approvals.)

Five bank holding companies (Citicorp, Bankers Trust, Chase, J.P. Morgan and Security Pacific) currently have applications pending before the Board to underwrite and deal in corporate debt and equity securities of all types (except mutual fund shares) subject to the 5 percent revenue limitation and the firewalls in the Board's order. Notice of the applications has been published in the Federal Register requesting public comment. The comment period expires on December 8, 1988.

Federal Reserve Board Securities Orders

Securities Underwriting

The Federal Reserve Board has conditionally approved the following applications by bank holding companies to underwrite and deal in, to a limited extent, certain securities (municipal revenue bonds, mortgage-related securities, commercial paper or consumer-receivable-related securities).

-- Citicorp, New York, to underwrite and deal in municipal revenue bonds and mortgage-related securities through Citicorp Securities, Inc. (4/30/87)

-- J.P. Morgan & Co. Incorporated, New York, to underwrite and deal in municipal revenue bonds, mortgage-related securities and commercial paper through J.P. Morgan Securities Inc. and J.P. Morgan Municipal Finance Inc. (4/30/87)

-- Bankers Trust New York Corporation, New York, to underwrite and deal in municipal revenue bonds, mortgage-related securities and commercial paper through BT Securities Corporation (4/30/87)

-- Chemical New York Corporation, New York, to underwrite and deal in municipal revenue bonds, mortgage-related securities and commercial paper and to place third party commercial paper through Chemical Securities, Inc. (5/18/87)

-- The Chase Manhattan Corporation, New York, to underwrite and deal in municipal revenue bonds and mortgage-related securities through Chase Manhattan Securities, Inc. (5/18/87)

-- Citicorp, New York, to underwrite and deal in commercial paper through Citicorp Securities, Inc. (5/18/87)

-- Manufacturers Hanover Corporation, New York, to underwrite and deal in municipal revenue bonds, mortgage-related securities and commercial paper and to place commercial paper through Manufacturers Hanover Securities Corporation (5/18/87)

-- Security Pacific Corporation, Los Angeles, to underwrite and deal in municipal revenue bonds, mortgage-related securities and commercial paper through Security Pacific Securities, Inc. (5/18/87)

- PNC Financial Corp, Pittsburgh, to underwrite and deal in municipal revenue bonds and commercial paper through PNC Investment Company (7/1/87)
- Chemical New York Corp., The Chase Manhattan Corp., Bankers Trust New York Corp., Citicorp, Manufacturers Hanover Corp., Security Pacific Corp., to underwrite and deal in consumer-receivable-related securities (7/14/87)
- Marine Midland Banks, Incorporated, Buffalo, to underwrite and deal in municipal revenue bonds, mortgage-related securities, commercial paper and consumer-receivable-related securities through Marine Midland Capital Markets Corporation (7/14/87)
- J.P. Morgan & Co. Incorporated to underwrite and deal in consumer-receivable-related securities (9/8/87)
- First Interstate Bancorp, Los Angeles, to underwrite and deal in municipal revenue bonds, mortgage-related securities, and commercial paper through First Interstate Capital Markets, Inc. (10/7/87)
- Bank of New England Corporation, Boston, to underwrite and deal in municipal revenue bonds, mortgage-related securities, commercial paper and consumer-receivable-related securities and to place commercial paper through BNE Capital Market Company (12/14/87)
- The Chase Manhattan Corporation, New York, to underwrite and deal in commercial paper through Chase Manhattan Treasury Corporation, New York, (same as Chase Manhattan Securities, Inc.) (4/27/88)
- The Bank of Montreal, Toronto, Canada, to underwrite, deal in and place commercial paper through Nesbitt Thomson Securities, Inc., New York (5/25/88)
- First Chicago Corporation, Chicago, Illinois, to underwrite and deal in mortgage-related securities, municipal revenue bonds, commercial paper and consumer-receivable-related securities through First Chicago Capital Markets, Inc., Chicago, Illinois (8/4/88)
- Bank of Boston Corporation, Boston, Massachusetts, to underwrite and deal in mortgage-related securities, municipal revenue bonds, commercial paper and consumer-receivable-related securities through BancBoston Securities, Inc., Boston, Massachusetts (8/8/88)

-- Fleet/Norstar Financial Group, Inc., Providence, Rhode Island, and Fleet/Norstar New York, Inc., Albany, New York, to underwrite and deal in municipal revenue bonds and commercial paper through Adams, McEntee & Co., Inc., New York, New York (10/3/88)

-- CoreStates Financial Group, Philadelphia, Pennsylvania, to underwrite and deal in mortgage-related securities, municipal revenue bonds, commercial paper and consumer-receivable-related securities through CoreStates Securities Corp., Philadelphia, Pennsylvania (10/11/88)

Additional Approvals

The Board has also approved applications by The Chase Manhattan Corporation to underwrite and deal in commercial paper through Chase Commercial Corporation (a commercial lending subsidiary) (3/18/87) and to underwrite and deal in mortgage-backed securities through Chase Home Mortgage Corporation (a mortgage lending subsidiary) (7/17/87). Unlike the underwriting cases listed above, these cases did not involve subsidiaries that underwrite and deal in government securities and hence did not raise the same set of issues.

The most likely result however will be legislation to curb hostile takeover abuses, and possibly legislation clarifying the laws on insider trading.

Transaction Taxes

Speaker Jim Wright publicly called for consideration of a transaction tax on securities markets. The futures industry has little doubt that were such a tax to proceed, it would lead to a tax on the futures transactions as well. Their feeling is that any such transactions tax could greatly diminish volume and harm our capital markets, now the strongest in the world. Their view is that trading is a voluntary activity and a tax could greatly diminish trading activity, and/or simply lead to the trading being accomplished in Tokyo, London, or other major exchanges around the world. In this day of satellite computer feeds, traders can seek any market and will do so with a cost incentive.

Enclosed are articles regarding program trading and exchange rates.