

NASD Notice to Members 98-48

SEC Approves Amendments To Free- Riding And Withholding Interpretation; Effective August 17, 1998

Suggested Routing

- ☒ Senior Management
- ☐ Advertising
- ☒ Continuing Education
- ☒ Corporate Finance
- ☐ Executive Representatives
- ☐ Government Securities
- ☒ Institutional
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- ☐ Registration
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- ☒ Syndicate
- ☐ Systems
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- ☐ Variable Contracts

Executive Summary

On May 18, 1998, the Securities and Exchange Commission (SEC) approved amendments to National Association of Securities Dealers, Inc. (NASD[®]) Interpretive Material 2110-1 (IM-2110-1) and Rule 2720, revising certain provisions of the Free-Riding and Withholding Interpretation (Interpretation). These amendments address direct and indirect owners of broker/dealers, investment grade debt offerings, foreign investment companies, secondary offerings, issuer directed share programs, and accounts under the Employment Retirement Income Security Act. The amendments also provide NASD Regulation, Inc., staff with general exemptive authority. These rule amendments will be effective on August 17, 1998. The text of the amended rules and the *Federal Register* version of the SEC approval order are attached. This *Notice* is being issued to alert members of their revised compliance responsibilities under the Interpretation.

Questions concerning this *Notice* should be directed to Gary L. Goldsholle, Assistant General Counsel, Office of General Counsel, NASD RegulationSM, at (202) 728-8104.

Background

The purpose of the Interpretation is to protect the integrity of the public offering system by ensuring that members make a bona fide public distribution of "hot issue" securities and do not withhold such securities for their own benefit or use such securities to reward persons who are in a position to direct future business to the member. Hot issue securities are defined by the Interpretation as securities of a public offering that trade at a premium in the secondary market whenever such trading commences. The Interpretation also assures that members and partici-

pants in the securities industry do not take unfair advantage of their "insider position" in the industry to the detriment of public investors.

The Interpretation prohibits members from retaining the securities of hot issues in their own accounts and prohibits members from allocating such securities to directors, officers, employees, and associated persons of such members and other broker/dealers. It also restricts member sales of hot issue securities to the accounts of specified categories of persons, including, among others, senior officers of banks, insurance companies, investment companies, investment advisory firms, or any other institutional type account, and any other person with such organizations whose activities influence or include the buying and selling of securities. These basic prohibitions and restrictions are also made applicable to sales by members to accounts in which any such persons may have a beneficial interest and, with some exceptions, to members of the immediate family of those persons restricted by the Interpretation.

Amended Rules

NASD Regulation has received SEC approval of amendments to IM-2110-1 and Rule 2720. See 63 FR 28535 (May 26, 1998). These amendments provide for the following:

Exemptive Authority

New paragraph (a)(5) of the Interpretation provides NASD Regulation staff with general exemptive authority. As revised, the Interpretation authorizes NASD Regulation staff, upon written request made by a member, pursuant to the Rule 9600 Series, to provide an exemption unconditionally or on specified terms from any or all provisions, consistent with the purposes of the Interpretation, the protection of investors, and

the public interest. Persons requesting an exemption from the Interpretation should submit a detailed written statement of the grounds for granting the exemption to: NASD Regulation, Inc., Attn: Office of General Counsel, 1735 K Street, N.W., Washington, DC 20006.

Treatment Of Direct And Indirect Owners Of Broker/Dealers

New paragraph (b)(9) addresses persons who directly or indirectly have an ownership interest in a broker/dealer, other than a limited business broker/dealer as defined in paragraph (c) of the Interpretation. The subparagraph creates a new category of restricted person, providing generally that members shall not sell hot issue securities to a person, or a member of the immediate family of such person who is supported directly or indirectly to a material extent by such person, who has contributed capital to a broker/dealer, other than solely a limited business broker/dealer, or the account in which any such person has a beneficial interest. The amendments provide an exemption from this new category for persons whose ownership interest is passive and less than 10 percent, and where either: (1) such person purchases hot issues from a person other than the member in which it has a passive ownership and such person is not in a position to direct the allocation of hot issues; or (2) the member in which such person has a passive ownership interest or the parent of such member is publicly traded on an exchange or The Nasdaq Stock MarketSM (Nasdaq[®]).

The provisions in new paragraph (b)(9) also provide an exemption for sales to the account of any person restricted under subparagraph (b)(9) that is established for the benefit of bona fide public customers, includ-

ing, among others, insurance company general, separate, and investment accounts, and bank trust accounts. Members should be aware that this exemption applies solely to the accounts of persons restricted pursuant to paragraph (b)(9). It should be noted that paragraph (b)(9) does not restrict purchases of hot issues by any entity owned in part or whole by the person restricted by paragraph (b)(9), but instead reaches only the "accounts" in which restricted owners have a beneficial interest.

Rated Investment Grade Debt

The amendments to the Interpretation exempt certain classes of debt securities. Specifically, the amendments exempt debt securities (other than debt securities convertible into common or preferred stock) and financing instrument-backed securities that are rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories. Members should be aware that debt securities and financing instrument-backed securities must *both* be rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories. NASD Regulation reminds members that the Interpretation will continue to apply to all other types of debt instruments, except those expressly excluded.

Foreign Investment Companies

The amendments to paragraphs (f) and (l)(6) of the Interpretation exempt sales of hot issues to foreign investment companies that meet the following criteria: (1) the fund has 100 or more investors; (2) the fund is listed on a foreign exchange or authorized for sale to the public by a foreign regulatory authority; (3) no more than 5 percent of the fund assets are to be invested in the hot

issue securities being offered; and (4) any person owning more than 5 percent of the shares of the fund is not a restricted person as described in paragraph (b)(1), (2), (3), (4), or (9) of the Interpretation. In order for a member to sell hot issues to a foreign investment company, as defined above, the member must receive a written certification prepared by counsel admitted to practice law before the highest court of any state of the United States or the foreign jurisdiction where the investment company is organized, or by an independent certified public accountant licensed in any state of the United States or the foreign jurisdiction where the investment company is organized.

The written certification made pursuant to paragraph (l)(6) shall be deemed current for the same period as certifications furnished pursuant to paragraph (f)(1)(B). Specifically, a written certification by counsel or an independent certified public accountant shall be deemed current if it is based upon the status of the account as of a date not more than 18 months prior to the date of the hot issue transaction.

For purposes of paragraph (l)(6), NASD Regulation interprets the provision that there be 100 or more investors to require that 100 or more persons have direct investments in the foreign investment company. NASD Regulation would not permit investors of an entity that in turn invests in the foreign investment company to be included in the total number of investors for purposes of paragraph (l)(6).

Secondary Distributions

The amendments also exempt certain secondary offerings from the Interpretation. The amendments to the definition of the term "public offering"¹ in paragraph (l)(1) exempt hot

issues in a secondary distribution by an issuer, or any security holder of the issuer, of “actively-traded securities.” New paragraph (l)(7)(A) defines “actively-traded securities” as securities that have an average daily trading volume (ADTV) of at least \$1 million and are issued by an issuer whose common equity securities have a public float of at least \$150 million. New paragraph (l)(7)(B) defines the term “ADTV.” The definitions of “actively-traded securities” and “ADTV” were modeled after the SEC’s Regulation M. 62 FR 520 (January 3, 1997).

Issuer-Directed Share Exemptions

Issuer-directed share programs have become an increasingly valuable and popular tool for employee development and retention. The amendments to paragraph (d) of the Interpretation are designed to simplify the application of the issuer-directed share exemption to employees and directors of an issuer. The amendments permit an issuer specifically to direct its own shares to employees and directors, or employees and directors of a parent or subsidiary of the issuer, or any other entity which controls or is controlled by the issuer, or potential employees and directors resulting from an intended merger, acquisition, or other business combination of the issuer. For purposes of this paragraph, a parent-subsidiary or other control relationship would be deemed to include an entity that holds 50 percent or more of any class of equity securities of another entity. Employees and directors of sister corporations to the issuer are not subject to an exemption for issuer-directed securities, however, members may request an exemption for such persons under paragraph (a)(5) as discussed above.

Members should note that the issuer-directed share program is no longer limited to persons restricted in paragraphs (b)(3) through (8) of the Interpretation. NASD Regulation’s amendments permit employees and directors of an issuer to purchase hot issues from such issuer’s directed share program even if such employees and directors are materially supported by persons associated with a member restricted under paragraph (b)(2) of the Interpretation.

The amendments also consolidate the issuer-directed share provisions in paragraph (d). Separate provisions addressing issuer-directed share programs of members and parents of members were contained in Rule 2720(m). The new provisions standardize the “lock-up” period for issuer-directed securities to three months.

NASD Regulation reminds members that the Interpretation is designed to ensure that members make a bona fide public distribution of hot issue securities of a public offering that trade at a premium in the secondary market regardless of whether such securities are acquired by the member as an underwriter, as a selling group member, or from a member participating in the distribution as an underwriter or a selling group member, or otherwise. These provisions ensure that the Interpretation applies to securities that are part of a public offering notwithstanding that some of those securities are specifically directed by the issuer on a non-underwritten basis. NASD Regulation will continue its practice of requiring the managing underwriter of the offering to be responsible for ensuring that the distribution of non-underwritten securities is made in compliance with the Interpretation.

As a result of the plenary exemptive authority granted in new paragraph (a)(5), NASD Regulation has elimi-

nated paragraph (d)(2) from the Interpretation. Members may request an exemption for the sale of issuer-directed securities to a restricted person who is neither an employee nor director of the issuer under the general exemptive procedures described above. While NASD Regulation staff will be able to exercise greater flexibility than currently permitted under the Interpretation, members should articulate a valid business reason for such sales. In addition, members should represent that such securities shall not be subject to the same “lock-up” provisions as securities directed by an issuer pursuant to paragraph (d).

Accounts For Qualified Plans Under The Employment Retirement Income Security Act (ERISA)

New paragraph (f)(3) addresses the status of qualified employee benefit plans under ERISA. Generally, the amendments provide that an employee benefits plan qualified under ERISA shall not be deemed restricted. The amendments in new paragraph (b)(3) provide guidance in determining the factual circumstances in which a qualified ERISA plan would be deemed restricted.

Questionnaire

In its review for compliance with the Interpretation, NASD Regulation regularly issues a Free-Riding Questionnaire through the Compliance Desk software service to the managing underwriter and other members participating in the distribution of hot issue securities. NASD Regulation has revised the questionnaire to reflect the amendments to the Interpretation. A copy of the new Questionnaire follows this *Notice*. Additional information about the Compliance Desk and the Questionnaire is contained in *Notice to Members 96-18*.

Text Of Rule Amendments

(Note: Next text is underlined; deletions are bracketed.)

IM-2110-1. Free-Riding and Withholding

(a) Introduction

(1) No change.

(2) As in the case of any other interpretation issued by the [Board of Governors of the] Association, the implementation thereof is a function of the NASD Regulation staff [District Business Conduct Committee] and the [Board of Governors] NASD Regulation Board of Directors. Thus, the interpretation will be applied to a given factual situation by NASD Regulation staff, subject to oversight by the Board, with staff soliciting input from individuals active in the investment banking and securities business [who are serving on these committees or on the Board. They]. In making such interpretations, staff and the Board will construe this interpretation to effectuate its overall purpose to assure a public distribution of securities for which there is a public demand.

(3)-(4) No change.

(5) The NASD Regulation staff, upon written request, may, taking into consideration all relevant factors, provide an exemption either unconditionally or on specified terms from any or all of the provisions of this interpretation upon a determination that such exemption is consistent with the purposes of the interpretation, the protection of investors, and the public interest. A member may appeal a decision issued by NASD Regulation staff to the National Adjudicatory Council pursuant to the Code of Procedure.

(b) Violations of Rule 2110

(1)-(8) No Change

(9) Sell any of the securities to any person, or to a member of the immediate family of such person who is supported directly or indirectly to a material extent by such person, who owns or has contributed capital to a broker/dealer, other than solely a limited business broker/dealer as defined in paragraph (c) of this interpretation, or the account in which any such person has a beneficial interest, provided, however, that:

(A) The prohibition shall not apply to any person who directly or indirectly owns any class of equity securities of, or who has made a contribution of capital to, a member, and whose ownership or capital interest is passive and is less than 10% of the equity or capital of a member, as long as:

(i) such person purchases hot issues from a person other than the member in which it has such passive ownership and such person is not in a position by virtue of its passive ownership interest to direct the allocation of hot issues, or

(ii) such member's shares or shares of a parent of such member are publicly traded on an exchange or Nasdaq.

(B) This prohibition shall not apply to sales to the account of any person restricted under this subparagraph (9) established for the benefit of bona fide public customers, including insurance company general, separate and investment accounts, and bank trust accounts.

(C) For purposes of this subparagraph (9), any person with an equity ownership or capital interest in an entity that maintains an investment in a member shall be deemed to have

a percentage interest in the member equal to the percentage interest of the entity in the member multiplied by the percentage interest of such person in such entity.

(c) No Change

(d) Issuer-Directed Securities

[(1) This interpretation shall apply to securities which are part of a public offering notwithstanding that some or all of those securities are specifically directed by the issuer to accounts which are included within the scope of paragraph (b)(3) through (8) above. Therefore, if a person within the scope of those subparagraphs to whom securities were directed did not have the required investment history, the member would not be permitted to sell him such securities. Also, the "disproportionate" and "insubstantial" tests would apply as in all other situations. Thus, the directing of a substantial number of securities to any one person would be prohibited as would the directing of securities to such accounts in amounts which would be disproportionate as compared to sales to members of the public. If such issuer-directed securities are sold to the issuer's employees or directors or potential employees or directors resulting from an intended merger, acquisition, or other business combination, such securities may be sold without limitation as to amount and regardless of whether such employees have an investment history as required by the interpretation; provided, however, that in the case of an offering of securities for which a bona fide independent market does not exist, such securities shall not be sold, transferred, assigned, pledged, or hypothecated for a period of three months following the effective date of the offering. This interpretation shall also apply to securities which are part of a public offering notwithstanding that some of those securities are

specifically directed by the issuer on a non-underwritten basis. In such cases, the managing underwriter of the offering shall be responsible for insuring compliance with this interpretation in respect to those securities.]

[(2) Notwithstanding the above, sales of issuer-directed securities may be made to non-employee/director restricted persons without the required investment history after receiving permission from the Board of Governors. Permission will be given only if there is a demonstration of valid business reasons for such sales (such as sales to distributors and suppliers, who are in each case incidentally restricted persons), and the member seeking permission is prepared to demonstrate that the aggregate amount of securities so sold is insubstantial and not disproportionate as compared to sales to members of the public, and that the amount sold to any one of such persons is insubstantial in amount; provided, however, that such securities shall not be sold, transferred, assigned, pledged, or hypothecated for a period of three months following the effective date of the offering.]

Employees and directors of an issuer, a parent of an issuer, a subsidiary of an issuer, or any other entity which controls or is controlled by an issuer, or potential employees and directors resulting from an intended merger, acquisition, or other business combination of an issuer otherwise subject to this interpretation in paragraphs (b)(2) through (9) may purchase securities that are part of a public offering that are specifically directed by the issuer to such persons; provided, however, that in the case of an offering of securities for which a bona fide independent market does not exist, such securities shall not be sold, transferred, assigned, pledged, or hypothecated for a period of three months

following the effective date of the offering.

(e) No Change

(f) Investment Partnerships and Corporations

(1) A member may not sell a hot issue to the account of any investment partnership or corporation, domestic or foreign (except companies registered under the Investment Company Act of 1940 or foreign investment companies as defined herein) including but not limited to hedge funds, investment clubs, and other like accounts unless the member complies with either of the following alternatives:

(A)-(B) No Change

(2) The member shall maintain a copy of the names and business connections of all persons having any beneficial interest in the account or a copy of the current written representation in its files for at least three years following the member's last sale of a new issue to the account, depending upon which of the above requirements the member elects to follow. For purposes of this paragraph (f) and the certification required pursuant to paragraph (l)(6), a list or written representation shall be deemed to be current if it is based upon the status of the account as of a date not more than 18 months prior to the date of the transaction.

(3) An employee benefits plan qualified under the Employee Retirement Income Security Act shall be deemed restricted under this interpretation in accordance with the following provisions:

(A) Any plan sponsored by a broker/dealer is restricted;

(B) Any plan sponsored by an entity that is not involved in financial ser-

vices activities is not restricted whether or not any plan participants may be restricted;

(C) Any plan sponsored by an entity that is engaged in financial services activities, including but not limited to, banks, insurance companies, investment advisers, or other money managers, is not restricted, provided that the plan permits participation by a broad class of participants and is not designed primarily for the benefit of restricted persons.

(g)-(k) No Change

(l) Explanation of Terms

The following explanation of terms is provided for the assistance of members. Other words which are defined in the By-Laws and Rules shall, unless the context otherwise requires, have the meaning as defined therein.

[(1) Associated Person

A person associated with a member or any other broker/dealer, as defined in Article I of the Association's By-Laws, shall not include a person whose association with the member is limited to a passive ownership interest in the member of 10% or less, and who does not receive hot issues from the member in which he or she has the ownership interest; and that such member is not in a position to direct hot issues to such person.]

[(2)1] Public Offering

The term public offering shall mean any primary or secondary distribution of securities made pursuant to a registration statement or offering circular including exchange offers, rights offerings, offerings made pursuant to a merger or acquisition, straight debt offerings, and all other securities distributions of any kind whatsoever

except any offering made pursuant to an exemption under Section 4(l), 4(2) or 4(6) of the Securities Act of 1933, as amended. The term public offering shall exclude exempted securities as defined in Section 3(a)(12) of the Act, and debt securities (other than debt securities convertible into common or preferred stock) and financing instrument-backed securities that are rated by a nationally recognized statistical rating organization in one of its four highest generic rating categories. The term public offering shall exclude secondary offerings by an issuer, or any security holder of the issuer, of actively-traded securities.

[(3)2] Immediate Family

The term immediate family shall include parents, mother-in-law or father-in-law, husband or wife, brother or sister, brother-in-law or sister-in-law, son-in-law or daughter-in-law, and children. In addition, the term shall include any other person who is supported, directly or indirectly, to a material extent by the member, person associated with the member or other person specified in paragraph (b)(2) above.

[(4)3] Normal Investment Practice

Normal investment practice shall mean the history of investment of a restricted person in an account or accounts maintained by the restricted person. Usually the previous one-year period of securities activity is the basis for determining the adequacy of a restricted person's investment history. Where warranted, however, a longer or shorter period may be reviewed. It is the responsibility of the registered representative effecting the allocation, as well as the member, to demonstrate that the restricted person's investment history justifies the allocation of hot issues. Copies of customer account statements or other records maintained

by the registered representative or the member may be utilized to demonstrate prior investment activity. In analyzing a restricted person's investment history the Association believes the following factors should be considered:

(A) The frequency of transactions in the account or accounts during that period of time. Relevant in this respect are the nature and size of investments.

(B) A comparison of the dollar amount of previous transactions with the dollar amount of the hot-issue purchase. If a restricted person purchases \$1,000 of a hot issue and his account revealed a series of purchases and sales in \$100 amounts, the \$1,000 purchase would not appear to be consistent with the restricted person's normal investment practice.

(C) The practice of purchasing mainly hot issues would not constitute a normal investment practice. The Association does, however, consider as contributing to the establishment of a normal investment practice, the purchase of new issues which are not hot issues as well as secondary market transactions.

[(5)4] Disproportionate

(A) In respect to the determination of what constitutes a disproportionate allocation, the Association uses a guideline of 10% of the member's participation in the issue, however acquired. It should be noted, however, that the 10% factor is merely a guideline and is one of a number of factors which are considered in reaching determinations of violations of the interpretation on the basis of disproportionate allocations. These other factors include, among other things:

(i) the size of the participation;

(ii) the offering price of the issue;

(iii) the amount of securities sold to restricted accounts; and

(iv) the price of the securities in the aftermarket.

(B) It should be noted that disciplinary action has been taken against members for violations of the interpretation where the allocations made to restricted accounts were less than 10% of the member's participation. The 10% guideline is applied as to the aggregate of the allocations.

(C) Notwithstanding the above, a normal unit of trading (100 shares or 10 bonds) will in most cases not be considered a disproportionate allocation regardless of the amount of the member's participation. This means that if the aggregate number of shares of a member's participation which is allocated to restricted accounts does not exceed a normal unit of trading, such allocation will in most cases not be considered disproportionate. For example, if a member receives 500 shares of a hot issue, he may allocate 100 shares to a restricted account even though such allocation represents 20% of the member's participation. Of course, all of the remaining shares would have to be allocated to unrestricted accounts and all other provisions of the interpretation would have to be satisfied. Specifically, the allocation would have to be consistent with the normal investment practice of the account to which it was allocated and the member would not be permitted to sell to restricted persons who were totally prohibited from receiving hot issues.

[(6)5] Insubstantiality

This requirement is separate and distinct from the requirements relating to disproportionate allocations and normal investment practice. In addition,

this term applies both to the aggregate of the securities sold to restricted accounts and to each individual allocation. In other words, there could be a substantial allocation to an individual account in violation of the interpretation and yet be no violation on that ground as to the total number of shares allocated to all accounts. The determination of whether an allocation to a restricted account or accounts is substantial is based upon, among other things, the number of shares allocated and/or the dollar amount of the purchase.

(6) Foreign Investment Company

The term foreign investment company shall include any fund company organized under the laws of a foreign jurisdiction, which has provided to the member a written certification prepared by counsel admitted to practice law before the highest court of any state of the United States or such foreign jurisdiction, or by an independent certified public accountant licensed to practice in any state of the United States or such foreign jurisdiction, that states that:

(A) the fund has 100 or more investors;

(B) the fund is listed on a foreign exchange or authorized for sale to the public by a foreign regulatory authority;

(C) no more than 5% of the fund assets are to be invested in the securities being offered; and,

(D) any person owning more than 5% of the shares of the fund is not a

restricted person as described in paragraphs (b)(1), (2), (3), (4) or (9) of this interpretation.

(7) Actively-traded securities

(A) Actively-traded securities means securities that have an ADTV value of at least \$1 million and are issued by an issuer whose common equity securities have a public float value of at least \$150 million.

(B) "ADTV" means the worldwide average daily trading volume, during the two full calendar months immediately preceding, or any 60 consecutive calendar days ending within the 10 calendar days preceding, the filing of the registration statement; or, if there is no registration statement or if the distribution involves the sale of securities on a delayed basis pursuant to Securities Act Rule 415, two full calendar months immediately preceding, or any consecutive 60 calendar days ending within the 10 calendar days preceding, the determination of the offering price.

(m) No Change

2720. Distribution of Securities of Members and Affiliates—Conflicts of Interest

(a)-(l) No Change

[(m) Sales to Employees—No Limitations

Notwithstanding the provisions of IM-2110-1, "Free-Riding and Withholding," a member may sell securities issued by a member, a parent of a member, an entity which wholly

owns a member, an entity which owns (alone or in the aggregate with any wholly-owned, non-public subsidiary) at least 51% of the outstanding voting stock of a member or by an issuer treated as a member or parent of a member under paragraph (i) hereof to the member's employees; potential employees resulting from an intended merger, acquisition, or other business combination of members resulting in one public successor corporation; persons associated with the member; and the immediate family of such employees or associated persons without limitation as to amount and regardless of whether such persons have an investment history with the member as required by IM-2110-1; provided, however, that in the case of an offering of equity securities for which a bona fide independent market does not exist, such securities shall not be sold, transferred, assigned, pledged, or hypothecated for a period of five months following the effective date of the offering.]

(n)-(q) are redesignated as (m)-(p)

Endnote

¹ The amendments to the definition of "public offering" apply only to the Interpretation and do not affect any other NASD rule, including Rules 2710, 2810, and 2720.

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NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Firm: _____

Address: _____

Re: _____ Offering Date: _____

INSTRUCTIONS: Each member is required to complete either Section I or Section II based upon the capacity in which they acted in the distribution of the new issue. Sections III and IV must be completed by all firms for their "confirmed"* securities. It is the executing broker/dealer's responsibility to ensure that securities were distributed in compliance with the Free-Riding and Withholding Interpretation, IM-2110-1.

SECTION I. TO BE COMPLETED BY THE MANAGING UNDERWRITER ONLY

- A. Total number of securities offered for public distribution: _____
(Include any additional shares sold as part of any over-allotment provision and any shares sold short for the account of the syndicate.)
- B. Total number of securities allocated for sale to other underwriters and selling group members: _____
- C. Total number of securities confirmed* by your firm to retail and institutional customers, including all shares billed and delivered on behalf of others, designated orders, group sales, directed sales, etc.: _____

SECTION II. TO BE COMPLETED BY ALL UNDERWRITERS, SELLING GROUP MEMBERS AND OTHER PARTICIPANTS IN THE DISTRIBUTION

- A. Total number of securities confirmed* by your firm to retail and institutional customers. (Do not include shares billed and delivered on your behalf by the managing underwriter, designated orders, group sales, directed sales, etc.):
- B. Indicate capacity in which your firm participated in the offering:
- ☐ Underwriter
- ☐ Selling Group
- ☐ Other (define) _____

* For purposes of this questionnaire, "confirmed" means the number of new issue securities allocated to the firm for distribution purposes and for which the firm has issued a confirmation/comparison reflecting the full detail of such sale to retail customers, institutional accounts, or other broker/dealers. When participating in a distribution of new issue securities, broker/dealers are responsible for ensuring compliance with the Free-Riding and Withholding Interpretation for all securities allocated and confirmed by that broker/dealer.

SECTION III. BREAKDOWN OF SECURITIES DISTRIBUTED BY YOUR FIRM

INSTRUCTIONS: Indicate total number of securities distributed in each category and, unless otherwise noted, provide detailed information in Section IV, "Sales to Restricted Accounts." This breakdown should contain the final figures after giving effect to all cancellations and reallocations. For additional information regarding categories, please refer to the Free-Riding and Withholding Interpretation, IM 2110-1.

1. Securities held in a firm account. _____

2. Sales to any officer, director, general partner, employee or agent of the member or any other broker/dealer, or to person associated with the member or with any other broker/dealer, or to a member of the immediate family of such a person. _____

Indicate the number of shares/units that were sold pursuant to the following provisions:

- (A) Sales to persons associated with broker/dealers whose business is limited to investment company/variable contract securities or direct participation programs.

Number of shares/units _____

- (B) Sales to a member of the immediate family of a person associated with a member who is not supported directly or indirectly by that person if the sale is by a broker/dealer other than that employing the restricted person and the restricted person has no ability to control the allocation of the hot issue.

Number of shares/units _____

It is not necessary to complete Section IV for items 2 (A) and (B).

3. Sales to a person who is a finder with respect to the public offering or to any person acting in a fiduciary capacity to the managing underwriter, including among others, attorneys, accountants and financial consultants, or to any other person who is supported directly or indirectly, to a material extent, by any person specified in this paragraph. _____

4. Sales to any senior officer of a bank, savings and loan institution, insurance company, investment company, investment advisory firm, or any other institutional type account, (including, but not limited to hedge funds, investment partnerships, investment corporations, or investment clubs) domestic or foreign, or to any person in the securities department of, or to any employee or any other person who may influence or whose activities directly or indirectly involve or are related to the function of buying and selling securities for any bank, savings and loan institution, insurance company, investment company, investment advisory firm, or other institutional type account, domestic or

foreign, or to any other person who is supported directly or indirectly, to a material extent, by any person specified in this paragraph. _____

5. Sales to any account in which any person specified under paragraphs (2), (3), or (4) has a beneficial interest. _____

6. Sales to other domestic broker/dealers for bona fide public customers, other than those enumerated in paragraphs (2), (3), (4), or (5) above. _____

Name of Broker/Dealer	No. of Shares/Units	Written Representation Received (pursuant to paragraph 6)	
		Yes	No
_____	_____	Yes	No
_____	_____	Yes	No
_____	_____	Yes	No

It is not necessary to complete Section IV for item 6.

7. Sales to any domestic bank, domestic branch of a foreign bank, trust company or other conduit for an undisclosed principal. _____

- (A) Indicate the number of shares/units that were sold based upon assurances obtained that ultimate purchasers were not restricted persons.
Number of shares/units _____

It is not necessary to complete Section IV for item 7(A).

8. Sales to a foreign broker/dealer or bank. _____

Indicate the number of shares/units that were sold pursuant to the following conditions.

- (A) Sales by a foreign broker/dealer or bank participating in the distribution as an underwriter that were made in accordance with provisions of underwriting agreement.
Number of shares/units _____
- (B) Affirmative inquiry was obtained that ultimate purchasers were not restricted persons.
Number of shares/units _____

It is not necessary to complete Section IV for items 8(A) and (B).

9. Sales to direct and indirect owners of a broker/dealer.

Indicate the number of shares/units that were sold pursuant to the following provisions.

- (A) Sales to direct and indirect owners whose passive ownership interest amounts to less than 10% of the broker/dealer, and:
- (1) the owner purchases hot issues from a person other than the member in which it has a passive ownership interest, and such owner is not in a position to direct the allocation of hot issues, or
Number of shares/units _____
- (2) the shares of the member or parent of the member in which the passive owner has an ownership interest are traded on an exchange or Nasdaq. _____
Number of shares/units _____
- (B) Sales to the account of any person restricted under paragraph (b)(9) of the Interpretation established for the benefit of bona fide public customers.
Number of shares/units _____

It is not necessary to complete Section IV for items 9(A) and (B).

10. Sales to an investment partnership or corporation, domestic or foreign (except companies registered under the Investment Company Act of 1940 or exempt foreign investment company as defined in the Free-Riding and Withholding Interpretation) including but not limited to hedge funds, investment clubs, and other like accounts.

Indicate the number of shares/units that were sold pursuant to the following conditions:

- (A) "Carve out" mechanism was utilized.
Number of shares/units _____
- (B) Determination was made based upon file containing information on all persons having a beneficial interest, or the opinion of counsel or accountants was obtained.
Number of shares/units _____

It is not necessary to complete Section IV for items 10(A) and (B).

11. Sales to public customers.

It is not necessary to complete Section IV for item 11.

TOTAL (1 through 11)

Please note that the total should be equal to total securities confirmed by your firm as noted in Section I or II.

Indicate the number of shares/units that were originally sold to a restricted account and were subsequently canceled prior to the end of the first business day after the date on which secondary market trading begins and were reallocated to an unrestricted account.

☐ Not Applicable

Signature of Principal

Title

NOTE: Questionnaires should be returned to the Corporate Financing Department by the date specified.

PLEASE NOTE THAT IN CERTAIN CIRCUMSTANCES AS SET FORTH IN THE INTERPRETATION, IT IS PERMISSIBLE TO SELL TO A RESTRICTED ACCOUNT. HOWEVER, IT IS THE OBLIGATION OF THE MEMBER TO DEMONSTRATE COMPLIANCE WITH THE APPLICABLE PROVISIONS OF THE INTERPRETATION.

REPORTING MEMBER _____

ISSUE: _____

DATE OF PUBLIC OFFERING: _____

[illegible]

SALES ARE PERMITTED TO MEMBERS OF THE IMMEDIATE FAMILY PROVIDED THAT SUCH PERSONS DO NOT CONTRIBUTE DIRECTLY OR INDIRECTLY TO THE SUPPORT OF SUCH MEMBER OF THE IMMEDIATE FAMILY. SECURITIES WERE SOLD TO SUCH PERSONS IN ACCORDANCE WITH THEIR NORMAL INVESTMENT PRACTICE AND THAT THE AGGREGATE OF THE SECURITIES SO SOLD IS INSUBSTANTIAL AND NOT DISPROPORTIONATE TO DEMONSTRATE INVESTMENT HISTORY AT YOUR FIRM OR ANOTHER BROKERO DEALER. PLEASE SUBMIT A TRANSCRIPT OR OTHER EVIDENCE FOR EACH ACCOUNT. TRANSCRIPT SHOULD INCLUDE ACCOUNT'S PRACTICE PRIOR TO OFFERING (I.E. 1 YEAR).

SALES OF ISSUER-DIRECTED SECURITIES, SALES PURCHASED PURSUANT TO A STAND-BY ARRANGEMENT AND SALES TO VENTURE CAPITAL INVESTORS, ARE NOT SUBJECT TO PROVISIONS OF THE INTERPRETATION PROVIDED THE CONDITIONS STIPULATED IN THE INTERPRETATION ARE MET.