

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The Commission believes MSTC's proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to registered transfer agents. The proposed rule change will allow MSTC to comply with Commission Rule 17Ad-16 which, among other things, require each qualified registered securities depository to provide its participants the notices it receives from transfer agents, directly or through the appropriate qualified registered security depository, when the transfer agent is terminating or assuming transfer agent services on behalf of an issuer or changing its name or address. Rule 17Ad-16 became effective on February 6, 1995.

MSTC also has requested that the Commission find good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of the filing in the **Federal Register**. Accelerated approval will permit MSTC to comply immediately with the requirements of Rule 17Ad-16. Thereby, the Commission finds good cause for so approving the proposed rule change.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying at the Commission's Public Reference Section, 450 Fifth Street, NW., Washington, DC 20549. Copies of such filings will also be available for inspection and copying at the principal office of the above-referenced self-regulatory organization. All submissions should refer to the File No. SR-MSTC-95-02 and should be submitted by March 15, 1995.

It is therefore ordered, pursuant to Section 19(b)(2) that the proposed rule

change (File No. SR-MSTC-95-02) is hereby approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁶

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34-35391; File No. SR-NASD-94-62, Amendment No. 1]

Self-Regulatory Organizations; Notice of Filing of Amendment No. 1 to Proposed Rule Change by National Association of Securities Dealers, Inc., Relating to Limit Order Protection for Member-to-Member Limit Order Handling on Nasdaq

February 16, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on February 15, 1995, the National Association of Securities Dealers, Inc. ("NASD" or "Association") filed with the Securities and Exchange Commission ("SEC" or "Commission") an amendment to the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the NASD. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The NASD proposes to amend SR-NASD-94-62 relating to limit order protection for member-to-member limit order handling in the Nasdaq Stock Market. Currently, the NASD's Interpretation to the Rules of Fair Practice¹ makes it a violation of just and equitable principles of trade for a member firm to trade ahead of its own customer's limit orders. In this amendment to its proposed expansion of the Interpretation, the NASD is proposing to amend the Interpretation to clarify that the "terms and conditions" exception to the Interpretation applies only to limit orders from institutional accounts, whether such limit orders come from a firm's own customers or are member-to-member limit orders. The term "institutional account" is defined in Article III, Section 21(c)(4) of the Rules of Fair Practice. Below is the text of the proposed rule change. Proposed new language, including the language

⁶ 17 CFR 200.30-3(a)(12) (1994).

¹ NASD Manual, Rules of Fair Practice, Art. III, Sec. 1 (CCH) ¶ 2151.07.

that was added in the original proposal, is italicized; language to be deleted is bracketed.

Limit Order Protection Interpretation to Article III, Section 1 of the NASD Rules of Fair Practice

To continue to ensure investor protection and enhance market quality, the NASD Board of Governors is issuing an Interpretation to the Rules of Fair Practice dealing with member firm treatment of [their] customer limit orders in Nasdaq securities. This Interpretation will require members acting as market makers to handle [their] customer limit orders with all due care so that market makers do not "trade ahead" of those limit orders. *Thus, members acting as market makers that handle customer limit orders, whether received from their own customers or from another member, are prohibited from trading at prices equal or superior to that of the limit order without executing the limit order, provided that, prior to September 1, 1995, this prohibition shall not apply to customer limit orders that a member firm receives from another member firm and that are greater than 1,000 shares. Such orders shall be protected from executions at prices that are superior but not equal to that of the limit order.* In the interests of investor protection, the NASD is eliminating the so-called disclosure "safe harbor" previously established for members that fully disclosed to their customers the practice of trading ahead of a customer limit order by a market-making firm.

Interpretation

Article III, Section 1 of the Rules of Fair Practice states that:

A member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade.

The Best Execution Interpretation states that: In any transaction for or with a customer, a member and persons associated with a member shall use reasonable diligence to ascertain the best inter-dealer market for the subject security and buy or sell in such a market so that the resultant price to the customer is as favorable as possible to the customer under prevailing market conditions. Failure to exercise such diligence shall constitute conduct inconsistent with just and equitable principles of trade in violation of Article III, Section 1 of the Rules of Fair Practice.

In accordance with Article VII, Section 1(a)(2) of the NASD By-Laws, the following interpretation under Article III, Section 1 of the Rules of Fair

Practice has been approved by the Board.

A member firm that accepts and holds an unexecuted limit order from a customer (whether its own customer or a customer of another member) in a Nasdaq security and that continues to trade the subject security for its own market-making account at prices that would satisfy the customer's limit order, without executing that limit order [under the specific terms and conditions by which the order was accepted by the firm], shall be deemed to have acted in a manner inconsistent with just and equitable principles of trade, in violation of Article III, Section 1 of the Rules of Fair Practice, provided that, until September 1, 1995, customer limit orders in excess of 1,000 shares received from another member firm shall be protected from the market maker's executions at prices that are superior but not equal to the limit order, and provided further, that a member firm may negotiate specific terms and conditions applicable to the acceptance of limit orders only with respect to limit orders for customer accounts that meet the definition of an "institutional account" as that term is defined in Article III, Section 21(c)(4) of the Rules of Fair Practice. Nothing in this section, however, requires members to accept limit orders from any customer[s].

By rescinding the safe harbor position and adopting this Interpretation of the Rules of Fair Practice, the NASD Board wishes to emphasize that members may not trade ahead of customer limit orders in their market-making capacity even if the member had in the past fully disclosed the practice to its customers prior to accepting limit orders. The NASD believes that, pursuant to Article III, Section 1 of the Rules of Fair Practice, members accepting and holding unexecuted customer limit orders owe certain duties to their customers and the customers of other member firms that may not be overcome or cured with disclosure of trading practices that include trading ahead of the customer's order. The terms and conditions under which institutional account customer limit orders are accepted must be made clear to customers at the time the order is accepted by the firm so that trading ahead in the firms' market making capacity does not occur. For purposes of this Interpretation, a member that controls or is controlled by another member shall be considered a single entity so that if a customer's limit order is accepted by one affiliate and forwarded to another affiliate for execution, the firms are considered a single entity and the market making unit may not trade ahead of that customer's limit order.

The Board also wishes to emphasize that all members accepting customer limit orders owe those customers duties

of "best execution" regardless of whether the orders are executed through the member's market making capacity or sent to another member for execution. As set out above, the best execution Interpretation requires members to use reasonable diligence to ascertain the best inter-dealer market for the security and buy or sell in such a market so that the price to the customer is as favorable as possible under prevailing market conditions. The NASD emphasizes that the order entry firms should continue to routinely monitor the handling of their customers' limit orders regarding the quality of the execution received.

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II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the NASD included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The NASD has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

The purpose of the amendment to the proposed rule change is to clarify that the Interpretation's "terms and conditions" exception to the protection of customer limit orders, whether the order is from a member's own customer or is a customer limit order sent to it for execution from another member (so-called "member-to-member" limit orders), is intended to apply only to limit orders from institutional accounts as that term is defined in Article III, Section 21(c)(4) of the Rules of Fair Practice. The background and rationale for this amendment to the proposed rule change are discussed below.

On December 23, 1994, the Commission published for comment the NASD's proposed rule to expand the scope of limit order protection beyond that presently afforded by member firms to their customers in the Nasdaq Stock Market.² The NASD's current Interpretation to the Rules of Fair Practice makes it a violation of just and equitable principles of trade for a member firm to trade ahead of its own

customer's limit orders. The proposal before the Commission now would extend this protection to limit orders from a customer of a firm that sends that customer's limit order to another member for execution (so-called "member-to-member" limit orders). In addition, the proposal has a phase-in period until September 1, 1995, in which a firm receiving a member-to-member limit order of greater than 1,000 shares would be prohibited from trading for its own account at prices that are superior but not equal to the limit order price. The NASD's proposal also maintained language from the existing Interpretation regarding the member's ability to negotiate with any customer specific terms and conditions regarding its acceptance of limit orders, provided that the member makes these conditions clear to the customer. It is that language that this amendment is intended to affect.

The NASD believes that it is necessary to clarify that the terms and conditions exception to the handling of limit orders is intended to apply only to customer orders from institutional accounts as that term is defined in Article III, Section 21(c)(4) of the Rules of Fair Practice. Using that definition, a firm could negotiate limit order terms and conditions if the order came from:

- Banks, savings and loan associations, insurance companies, or registered investment companies;
- Investment advisers registered under Section 203 of the Investment Advisers Act of 1940; and
- Any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$50 million.

Accordingly, under the amended language, a member firm that accepts a limit order from a person or entity that does not fall within the definition of institutional account may not initiate the negotiation of any terms and conditions on the acceptance of that limit order. On the other hand, if the account placing the limit order meets the terms of the definition of institutional account, the firm may negotiate special terms and conditions with the customer of that account, or its representative, that permit the firm to trade ahead of or at the same price as the limit order. The amended Interpretation would apply to limit orders placed by the firm's own customers and member-to-member limit orders.

The NASD believes that this approach should minimize a retail customer's potential for confusion regarding the acceptance of a limit order that, under the existing Interpretation, could have

² Securities Exchange Act Release No. 35122 (Dec. 20, 1994), 59 FR 66389 (Dec. 23, 1994).

qualified the protection of the limit order rule's scope. At the same time, the amendment accurately reflects the ordinary framework in which firms and institutions typically negotiate the conditions under which an institution's limit order is to be handled. For example, in its approval of the original NASD Interpretation regarding the handling of customer limit orders,³ the Commission specifically indicated its view that the terms and conditions language of the original NASD Interpretation was included to permit special treatment for institutional customer limit orders. In addition, in its own proposal regarding customer limit order protection for Nasdaq National Market securities, proposed Rule 15c5-1,⁴ the Commission solicited comment on the "terms and conditions" provisions in its rule, which would allow the parties to a trade to set special conditions to allow a market maker to employ an appropriate strategy in filling an institutional customer's order without violating the proposed rule. Of course, the clarification of the Interpretation continues to permit a member to establish with its customers or the order entry firm commissioner or commission equivalents regarding the handling of a limit order, provided that the member makes these charges clear to the customer. In this connection, the NASD notes that Nasdaq market makers are free to negotiate additional compensation from order routing firms to the extent that such compensation is economically and competitively justified. Similarly, the Interpretation continues in place the understanding that nothing in the Interpretation would obligate a market maker to accept limit orders from any or all customers or member firms.

The NASD believes that the proposed rule change is consistent with section 15A(b)(6) of the Act in that these proposed changes are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to facilitate transactions in these securities, to remove impediments to and to perfect the mechanism of a free and open market and a national market system, and in general to protect investors and the public interest.

(B) Self-Regulatory Organization's Statement on Burden on Competition

The NASD does not believe that the proposed rule change will result in any

burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended. Accordingly, while the NASD will monitor carefully for any adverse competitive effects of the Interpretation, it believes that any adverse effects are far outweighed by the enhanced execution opportunities provided public investors.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the NASD consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to SR-NASD-94-62, Amendment No. 1 and should be submitted by March 7, 1995.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34-35376; File No. SR-Phlx-095-11]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc., Relating to the Listing of Five Year Long-Term Index Options

February 14, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 73s(b)(1), notice is hereby given that on February 8, 1995, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Phlx, pursuant to Rule 19b-4 of the Act, proposes to amend its Rule 1101A to permit the listing of index option series with up to 60 months (five years) until expiration. Currently, Rule 1101A permits "long-term" options up to 36 months until expiration.¹ The text of the proposed rule change is available at the Office of the Secretary, the Phlx, and at the Commission.

II. Self-Regulatory Organization's Statement of the Purpose of and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Phlx included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Phlx has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.

¹ See Rule 1101A(b)(iii).

³ See Securities Exchange Act Release No. 34279 (June 29, 1994), 59 FR 34883 (July 7, 1994).

⁴ See Securities Exchange Act Release No. 34753 (Sept. 29, 1994), 59 FR 50866 (Oct. 6, 1994).