

also be adjusted, if necessary, in the event of a merger, consolidation, dissolution, or liquidation of an issuer or in certain other events such as the distribution of property by an issuer to shareholders, the expropriation or nationalization of a foreign issuer, or the imposition of certain foreign taxes on shareholders of a foreign issuer. Shares of a component security may be replaced (or supplemented) with other securities under certain circumstances, such as the conversion of a component security into another class of security, the termination of a depositary receipt program, or the spin-off of a subsidiary. If the security remains in the Index, the number of shares of that security may be adjusted, to the nearest whole share, to maintain the component's relative weight in the Index at the level immediately prior to the corporate action.⁶ In all cases, the divisor will be adjusted, if necessary, to ensure continuity of the value of the Index.

The value of the Index will be calculated continuously by the Amex and disseminated every 15 seconds over the Consolidated Tape Association's Network B.

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act, in general, and furthers the objectives of Section 6(b)(5) in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system.

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

The Ampex does not believe that the proposed rule change will impose any inappropriate burden on competition.

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

No written comments were solicited or received with respect to the proposed rule change.

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)

⁶Lehman will not attempt to find a replacement stock or compensate for the extinction of a security due to bankruptcy or a similar event.

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 self-regulatory organization 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, 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 in the Commission's Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. Copies of such filing will also be available for inspection and copying at the principal office of the Amex. All submissions should refer to File No. Sr-Amex-95-21 and should be submitted by July 7, 1995.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁷

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95-14794 Filed 6-15-95; 8:45 am]

BILLING CODE 8010-01-M

[Release No. 34-35837; File No. SR-NYSE-94-45]

Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Granting Approval to Proposed Rule Change Relating to Member Organization Facilitation of a Customer Stock or Program Orders

June 12, 1995.

I. Introduction

On December 6, 1995, the New Stock Exchange, Inc. ("NYSE" or "Exchange") submitted to the Securities and Exchange Commission ("SEC" or

⁷ 17 CFR 200.30-3(a)(12) (1994).

"Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change regarding member organization facilitation of customer stock or program orders.³ On January 11, 1995, the Exchange submitted Amendment No. 1 to the proposed rule change.⁴

The proposed rule change was published for comment in Securities Exchange Act Release No. 35230 (January 13, 1995), 69 FR 4453 (January 23, 1995). One comment letter was received on the proposal.⁵

II. Description of Proposal

The NYSE proposal consists of an Information Memorandum to advise Exchange members of certain activities that the Exchange will consider inconsistent with just and equitable principles of trade. Specifically, the Memorandum discusses facilitation of customer block orders at the close, trading based upon information of imminent customer transactions, and procedures to review facilitation activities for compliance with Exchange rules and federal securities laws.

First, the Memorandum discusses a member's responsibilities when positioning itself to facilitate a customer transaction to be executed after the close at the closing price.⁶ The Memorandum states that a member should not trade for its own account "near the close" if it intends to execute an "at the close" order⁷ that reasonably can be expected to affect the closing price of the security. Whether or not the purchase will be deemed near the close will depend upon the degree of risk that reasonably

¹ 15 U.S.C. 78s(b)(1) (1988).

² 17 CFR 240.19b-4 (1994).

³ NYSE Rule 80A defines the term "program trading" as (1) index arbitrage or (2) any trading strategy involving the related purchase or sale of a "basket" or group of 15 or more stocks having a total market value of \$1 million or more.

⁴ See fax from Donald Siemer, NYSE, to Beth Stekler, SEC, dated January 11, 1995 (consisting of a revised Memorandum). The amendment made certain technical corrections to the text of the Memorandum.

⁵ See *infra* note 10 and accompanying discussion.

⁶ Although the Memorandum uses an example where the member has agreed to sell to a customer at the closing price, and therefore is purchasing stock before and at the close, the principles discussed in the Memorandum would apply equally to the situation where the member agrees to purchase stock from the customer at the closing price and therefore sells the security before and at the close. See letter from James Buck, Senior Vice President and Secretary, NYSE, to Brandon Becker, Director, Division of Market Regulation, SEC, dated April 19, 1995 ("NYSE Letter").

⁷ An "at the close order" is a market order which is to be executed in its entirety at the closing price on the Exchange. If the order is not executed at the closing price, it is treated as cancelled. See NYSE Rule 13.

could be attributed to the position established by the trade versus the reasonably anticipated impact the trade at the close will have on the closing price. Generally, however, trades after 3:40 p.m. will be considered executed "near the close."⁸

Second, the Memorandum states that if a member has knowledge of an imminent block order, the member should not effect any transactions in that stock with the intention of reversing the position subsequently by participating on the contra-side of the block transaction. The Memorandum further provides that a person should not disclose to any other person trading strategies or customers' orders so that the person may take advantage of the information for his or her personal benefit or for the benefit of the member organization.⁹

Finally, the Memorandum reminds members that they are required to establish and maintain procedures reasonably designed to review facilitation activities for compliance with Exchange rules and federal securities laws. It also states that members must ensure that trading strategies engaged in by their proprietary traders to facilitate customers' orders have an economic basis and are not engaged in to mark the close or to mark the value of a position, and that before any at the close customer orders are transmitted to the Floor of the Exchange, members accepting such orders must exercise due diligence to learn the essential facts relative to these orders.

III. Summary of Comments

The Commission received one comment letter on the proposed rule change on behalf of six NYSE-member firms (the "Comment Letter").¹⁰ The issues raised therein and the NYSE response are discussed below.¹¹

⁸The Memorandum notes that members will not be precluded from executing customer orders on an agency basis at any time, including at or near the close. The Memorandum, however, cautions that this does not preclude the Exchange from determining that such activity might be a violation of the anti-manipulation provisions of the Act or Exchange rules. See 15 U.S.C. 78i(a) and j(b) (1988); NYSE Rule 476.

⁹The Memorandum notes, however, that this would not preclude a member organization from soliciting interest to trade with the contra-side of a block in the normal course of engaging in block facilitation activities.

¹⁰ See letter from Roger Blanc, Willkie Farr & Gallagher, dated March 2, 1995 (representing Bear, Stearns & Co. Inc.; CS First Boston Corporation; Goldman, Sachs & Co.; Morgan Stanley & Co. Incorporated; PaineWebber Incorporated; and Saloman Brothers Inc.) ("Comment Letter").

¹¹ See NYSE Letter, *supra* note 6. According to the NYSE, the proposed rule change was reviewed and approved by the Exchange's Upstairs Traders

The Comment Letter noted that, because the rule change would preclude NYSE members from effecting proprietary transactions for the 20 minutes prior to the close, the proposal would result in additional risk for such members when facilitating customer block transactions at the closing price. As a result of this added risk exposure, it was argued that the costs to customers in executing such transactions would increase. In its response, the NYSE recognized that the proposal could produce additional risk for proprietary facilitation, but stated that the transactions after 3:40 p.m. bear *de minimis* risk because they are made in close proximity to a trade at the close that most likely would have a profitable impact on the prior transactions. In addition, the Exchange asserted that the rule change is consistent with the existing prohibitions against frontrunning, and that the 3:40 p.m. cut-off time was included to avoid confusion over what transactions generally would be considered "near the close."

The Comment Letter stated that the proposed rule appears to remove the Exchange's burden of proving manipulative intent on the part of a member that entered an order after 3:40 p.m., without "immunizing" transactions executed before that time. The Comment Letter asserted that because transactions occurring before 3:40 p.m. could still be deemed "near the close," the proposed rule change provides the Exchange with a high degree of prosecutorial discretion, making the proposal inconsistent with Section 6(b) (6) and (7) of the Act.¹² Additionally, the Comment Letter stated that predicated the prohibition against proprietary orders upon whether a member entered a market at the close order that "can reasonably be expected to impact the closing price" would require firms to predict the impact of future trades. The NYSE responded that it believes it is appropriate to use the proposed standard because it provides flexibility for judgmental errors. The NYSE also noted that this is the same standard used in frontrunning cases to assess compliance with just and equitable principles of trade.

Finally, the Comment Letter pointed out that the NYSE has not provided empirical support for restricting proprietary trading near the close. It also asserted that the transactions that would

Advisory Committee, Institutional Trading Advisory Committee, Market Performance Committee, and Quality of Markets Committee prior to filing with the Commission.

¹² 15 U.S.C. 78f(b) (6) and (7) (1988).

be prohibited represent actual customer demand, as opposed to orders by firms intended to take advantage of customer orders. The Comment Letter suggested that instead of the proposed interpretation, the Exchange should impose a requirement that members make full disclosure to their customers before undertaking transactions of this kind. In response, the Exchange stated that the empirical basis for its belief is demonstrated in patterns of trading that the Exchange has reviewed. The Exchange also asserted that disclosure to customers, even when the proprietary trade has a minimal impact, would be ineffective. According to the NYSE, the transactions in question may be effected due to the probability of immediate profitability, and they would, in any event, be based on an unfair informational advantage over other market participants. In addition, the NYSE asserted that, while the proprietary orders are initiated because of customer interest, those proprietary orders also would not be entered but for the knowledge of customer orders.

IV. Discussion

After careful consideration of the Comment Letter and the NYSE response thereto, the Commission has decided to approve the proposed rule change. For the reasons discussed below, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with the requirements of Sections 6(b) (5), (6), and (7).¹³

The Commission notes that two of the topics discussed in the Memorandum are restatements of current Exchange policy. Specifically, The Memorandum's discussion of trading based upon information of an imminent customer transaction and the requirement that members maintain procedures reasonably designed to review facilitation activities for compliance with Exchange rules and federal securities laws are consistent with Exchange Rule 476 and previous NYSE interpretations issued pursuant to that Rule.¹⁴ The Commission continues to believe that these policies are consistent with the Section 6(b)(5) requirement that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative

¹³ 15 U.S.C. 78f(b) (5), (6), and (7).

¹⁴ See, e.g., NYSE Information Memo Number 89-53 (November 27, 1989).

acts, and, in general, to protect investors and the public.

Similarly, the proposed Memorandum's description of the types of proprietary trading near the close that may, in certain circumstances, constitute a violation of just and equitable principles of trade is reasonably designed to address potential trading abuses that might occur when members are facilitating customer block or program orders. The Commission agrees with the NYSE that the conduct addressed in the Memorandum—trading with knowledge of impending large at the close orders—could prove detrimental to market integrity. The proposed guidelines for such trading near the close are consistent with long standing prohibitions against frontrunning. Moreover, the NYSE restrictions on block facilitation activities near the close are very limited in scope and should provide helpful guidance to members.

For the reasons discussed below, the Commission also believes the Comment Letter's criticisms of the proposal are adequately addressed. First, it is unnecessary for the NYSE to conduct further empirical studies before adopting this proposal. The NYSE represents that it has observed instances of block facilitation trading by its members that results in closing prices that disadvantage customers.¹⁵ In addition, as previously mentioned, the Memorandum is an elaboration of existing prohibitions against frontrunning. Thus, the NYSE is merely providing guidance on the types of conduct that already constitute a violation of just and equitable principles of trade under its rules.

Second, the Commission does not believe that simply requiring disclosure to customers sufficiently will protect customers or preserve market integrity. As the NYSE has indicated, the conduct addressed in this proposal affects not only the facilitation member's customer, but also all other market participants. The NYSE member still would have an informational advantage over the rest of the market even after full disclosure to its customer.

Third, the Comment Letter considers the Memorandum's guidance as a blanket prohibition against certain proprietary trading after 3:40 p.m., the designated cut-off time.¹⁶ The Memorandum, however, only restricts post-3:40 p.m. trading in limited circumstances. The Memorandum states that a member, when positioning itself to facilitate a customer transaction to be

made after the close at the closing price, should not trade for its own account "near the close" (after 3:40 p.m.) if it intends to execute an at the close order that reasonably can be expected to impact the closing price of the security. The Memorandum does not prohibit proprietary trading after 3:40 p.m., only a limited type of proprietary trading when in possession of a form of non-public, material market information.

Fourth, the Commission does not agree with the Comment Letter's assertion that the proposed regulation of proprietary trading near the close, defined generally as after 3:40 p.m., provides the Exchange with excessive prosecutorial discretion. The 3:40 p.m. cut-off is intended to provide members with *more* guidance as to prohibited conduct under the NYSE rules. At the same time, the 3:40 p.m. cut-off is not intended to operate as a "safe-harbor." The cut-off guideline provided in the Memorandum does not preclude the Exchange from determining that certain transactions before 3:40 p.m. were executed "near the close." The Commission agrees with the NYSE that the standard for determining which transactions are executed "near the close" must be flexible and take into consideration factors unique to the market for a particular security. The Commission therefore believes the proposed standard for determining when an execution is "near the close" is appropriate and even though it may cover transactions effected before the designated cut-off time.

Fifth, the Comment Letter suggests that the proposed standard would relieve the Exchange from proving manipulative intent for transactions executed after 3:40 p.m. The NYSE, however, seeks to address conduct that could enable block positioners to benefit from an unreasonable informational advantage over other market participants. The Commission believes that it is reasonable for the NYSE to adopt a position to reduce the likelihood of members trading to their own advantage based on customer information. This position still requires proof that the at the close order reasonably could be expected to affect the closing price.

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,¹⁷ that the proposed rule change (SR-NYSE-94-45) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁸

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95-14795 Filed 6-15-95; 8:45 am]

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[Release No. 34-35836; File No. SR-PSE-95-11]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Pacific Stock Exchange, Inc., Relating to the Number of Trading Posts That May Be Included as Part of Each Market Maker's Primary Appointment Zone

June 9, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on April 7, 1995, the Pacific Stock Exchange Incorporated ("PSE" 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 self-regulatory organization. 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 PSE proposes to increase the number of trading posts that may be included as part of each market maker's primary appointment zone.

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 self-regulatory organization 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 self-regulatory organization has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

¹⁵ See NYSE Letter, *supra* note 6.

¹⁶ See Comment Letter, *supra* note 10.

¹⁷ 15 U.S.C. 78s(b)(2) (1988).

¹⁸ 17 CFR 200.30-3(a)(12) (1994).

¹ 15 U.S.C. 78s(b)(1) (1988).