

Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of the proposal was published in the **Federal Register** On May 12, 1998.<sup>2</sup> No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

### I. Description

The rule change implements the HUB Mailbox service. The HUB Mailbox service will use the Institutional Delivery ("ID")<sup>3</sup> system's already-existing telecommunications facilities to allow investment managers and their custodians to exchange messages regarding: (1) securities purchases; (2) securities sales; (3) reconciliation data relating to securities positions and cash movements; and (4) other security-related transactions as agreed to by two or more HUB users. Occasionally, HUB users may also transmit trade data to recordkeeping vendors in situations where the custodial and accounting functions are performed by two different parties. All information will be entered in an ISITC<sup>4</sup> approved format initially, but other formats may be used later if agreed upon by two or more HUB users.<sup>5</sup>

To use the HUB Mailbox, investment managers and custodians will place

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> Securities Exchange Act Release No. 39955 (May 4, 1998), 63 FR 26237.

<sup>3</sup> For a complete description of the services provided by the ID system, refer to Securities Exchange Act Release Nos. 33466 (January 12, 1994), 59 FR 3139 [File No. SR-DTC-93-07] (order approving proposed rule change relating to the enhanced ID system); 34166 (June 6, 1994), 59 FR 31660 [File No. SR-DTC-94-01] (order approving proposed rule change to add a standing instruction database to the ID system institutional delivery system); 34199 (June 10, 1994) 59 FR 31660 [File No. SR-DTC-94-04] (order granting accelerated approval of a proposed rule change to implement the interactive capabilities and the electric mail features of the enhanced institutional delivery system); 36050 (August 2, 1995), 60 FR 41139 [File No. SR-DTC-95-10] (order approving proposed rule change implementing advice of confirm correction/cancellation feature and modifying the authorization/exception processing feature of the institutional delivery system); 39829 (April 6, 1998), 63 FR 17943 [File No. S7-10-98] (interpretation that a "matching" service that compares securities trade information from a broker-dealer's customer is a clearing agency function).

<sup>4</sup> ISITC (Industry Standardization for Institutional Trade Communication) is a global working committee of brokers, investment managers, custodians, and vendors which was established in 1991 and has developed standard message formats and operating protocols for transmitting information concerning security-related transactions.

<sup>5</sup> The notice of the proposed rule change, *supra* note 2, incorrectly stated that DTC developed the HUB Mailbox in cooperation with ISITC. It should have stated that DTC developed the HUB Mailbox service in cooperation with some ISITC members.

formatted records into bundles for each addressee with appropriately coded headers and trailers, and DTC will route the bundles to addressees' mailboxes for retrieval. Addressees will acknowledge receipt of bundles through their mailboxes. All mail messages, both delivered and undelivered, will be transferred at the end of each business day between 2:00 AM and 3:00 AM (ET) to a separate file which can be accessed directly on the next day. DTC will store mail messages for up to five days. The HUB Mailbox service will not do any processing other than to direct mail to appropriate mailboxes.

### II. Discussion

Section 17A(b)(3)(F) of the Act<sup>6</sup> requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions. As discussed below, the Commission believes that DTC's proposed rule change is consistent with this obligation.

The Commission believes that the electronic mail features of the HUB Mailbox service will enable users to reduce their reliance on facsimile transmissions when communicating information such as the details concerning securities purchases, sales, reconciliation, and other security related information. The Commission believes that transmitting this information electronically is more efficient and accurate than the methods currently used and therefore should help promote the prompt and accurate clearance and settlement of securities transactions.

### III. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular with Section 17A of the Act and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-DTC-98-02) be and hereby is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>7</sup>

**Jonathan G. Katz,**

*Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40227; File No. SR-NASD-98-01]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendments Nos. 1, 2, and 3 by the National Association of Securities Dealers, Inc. Relating to the NASD's Rules Regarding Electronic Communications Networks, Locked and Crossed Markets, and a Member's Obligation to Provide Nasdaq With Certain Information

July 17, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on January 27, 1998, the National Association of Securities Dealers, Inc. ("NASD"), through its wholly owned subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change. The NASD filed Amendment No. 1 to the proposal on June 8, 1998,<sup>2</sup> Amendment No. 2 on June 30, 1998,<sup>3</sup> and Amendment No. 3 on July 16, 1998.<sup>4</sup> The proposed rule change, as amended, is described in Items I, II, and III below, which Items have been prepared by Nasdaq. 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

Nasdaq is submitting proposed rule changes to amend NASD Rule 4623, which will specify the manner in which orders having a reserved size that are entered into an electronic communications network ("ECN") must interact with SelectNet orders. Additionally, Nasdaq is proposing to amend NASD Rule 4613(e) by adding a provision regarding locked and crossed markets that occur at the open. Nasdaq also is proposing the adoption of NASD Rule 4625, which will set out the obligation of members participating in

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> See letter from Robert E. Aber, Senior Vice President and General Counsel, The Nasdaq Stock Market, Inc. to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), SEC, dated June 5, 1998.

<sup>3</sup> See letter from Robert E. Aber, Senior Vice President and General Counsel, The Nasdaq Stock Market, Inc. to Katherine A. England, Assistant Director, Division, SEC, dated June 29, 1998.

<sup>4</sup> See letter from Robert E. Aber, Senior Vice President and General Counsel, The Nasdaq Stock Market, Inc. to Richard Strasser, Assistant Director, Division, SEC, dated July 15, 1998.

<sup>6</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>7</sup> 17 CFR 200.30-3(a)(12).

The Nasdaq Stock market to provide specified information to Nasdaq departments and staff when so requested. Proposed new language is italicized; proposed deletions are in brackets.

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#### Rule 4623. Electronic Communications Networks

(a) The Association may provide a means to permit electronic communications networks ("ECN"), as such term is defined in SEC Rule 11Ac1-1(a)(8), to meet the terms of the [electronic communications network] ECN display alternative provided for in SEC Rule 11Ac1-1(c)(5)(ii) (A) and (B) ("ECN display alternative"). In providing any such means, the Association shall establish a mechanism that permits the [electronic communications network] ECN to display the best prices and sizes of orders entered by Nasdaq market makers (and other entities, if the [electronic communications network] ECN so chooses) into the [electronic communications network] ECN, and allows any NASD member the electronic ability to effect a transaction with such priced orders that is equivalent to the ability to effect a transaction with a Nasdaq market maker quotation in Nasdaq operated systems.

(b) An [electronic communications network] ECN that seeks to utilize the Nasdaq-provided means to comply with the [electronic communications network] ECN display alternative shall:

(1) demonstrate to the Association that it qualifies as an [electronic communications network] ECN meeting the definition in the SEC Rule;

(2) be registered as a[n] NASD member;

(3) enter into and comply with the terms of a Nasdaq WorkStation Subscriber Agreement, *as amended for ECNs*;

(4) agree to provide for Nasdaq's dissemination in the quotation data made available to quotation vendors the prices and sizes of Nasdaq market maker orders (and other entities, if the [electronic communications network] ECN so chooses) at the highest buy price and the lowest sell price for each Nasdaq security entered in and widely disseminated by the [electronic communications network] ECN, and prior to entering such prices and sizes, register with Nasdaq Market Operations for each such security as an ECN; and

(5) provide an automated execution or, if the price is no longer available, an automated rejection of any order routed to the [electronic communications

network] ECN through the Nasdaq-provided display alternative.

(c) *When a NASD member attempts to electronically access through a Nasdaq-provided system an ECN-displayed order by sending an order that is larger than the ECN's Nasdaq-displayed size and the ECN is displaying the order in Nasdaq on a reserved size basis, the NASD member that operates the ECN shall execute such Nasdaq-delivered order:*

(1) *up to the size of the Nasdaq-delivered order, if the ECN order (including the reserved size and displayed portions) is the same size or larger than the Nasdaq-delivered order; or*

(2) *up to the size of the ECN order (including the reserved size and displayed portions), if the Nasdaq-delivered order is the same size or larger than the ECN order (including the reserved size and displayed portions).*

*No ECN operating in Nasdaq pursuant to this rule is permitted to provide a reserved-size function unless the size of the order displayed in Nasdaq is 100 shares or greater. For purposes of this rule, the term "reserved size" shall mean that a customer entering an order into an ECN has authorized the ECN to display publicly part of the full size of the customer's order with the remainder held in reserve on an undisplayed basis to be displayed in whole or in part as the displayed part is executed.*

#### Rule 4613 Character of Quotations

(a)-(d) No Change

(e) Locked and Crossed Markets

(1) A market maker shall not, except under extraordinary circumstances, enter or maintain quotations in Nasdaq during normal business hours if:

(A) the bid quotation entered is equal to or greater than the asked quotation of another market maker entering quotations in the same security; or

(B) the asked quotation is equal to or less than the bid quotation of another market maker entering quotations in the same security.

*The prohibitions of this rule include the entry of a locking or crossing quotation at or after 9:25 a.m. Eastern Time if such quotation continues to lock or cross the market at the market's opening, and requires a market maker or ECN that enters a locking or crossing quotation at or after 9:25 a.m. Eastern Time to take action to avoid the lock or cross at the market's open or immediately thereafter, but in no case more than 30 seconds after 9:30 a.m.*

(2) No Change

(3) For purposes of this [paragraph] rule, the term "market maker" shall include: any NASD member that enters into an [electronic communications network] ECN, as defined in SEC Rule 11Ac1-1(a)(8), a priced order that is displayed in The Nasdaq Stock Market; and [Such term also shall include] any NASD member that operates the [electronic communication network] ECN when the priced order being displayed has been entered by a person or entity that is not a[n] NASD member.

#### Rule 4625. Obligation to Provide Information

(1) A NASD member operating in or participating in the third market. The Nasdaq Stock Market, or other Nasdaq-operated system, shall provide information orally, in writing, or electronically (if such information is, or is required to be, maintained in electronic form) to the staff of Nasdaq when:

(a) Nasdaq MarketWatch staff makes an oral, written, or electronically communicated request for information relating to a specific NASD rule, SEC rule, or provision of a joint industry plan (e.g., ITS, UTP, CTA, and CQA) (as promulgated and amended from time-to-time) that Nasdaq MarketWatch is responsible for administering or to other duties and/or obligations imposed on Nasdaq MarketWatch by the Association under the Plan of Allocation and Delegation of Function by the NASD to Subsidiaries or otherwise; this shall include, but not be limited to, information relating to:

(i) a locked or crossed market;

(ii) a trade reported by a member or ECN to the Automated Transaction Confirmation Service ("ACT"); or

(iii) trading activity, rumors, or information that a member may possess that may assist in determining whether there is a basis to initiate a trading halt, pursuant to NASD Rule 4120 and IM-4120-1; or

(iv) a quotation that appears not to be reasonably related to the prevailing market.

(b) Nasdaq Market Operations staff makes an oral, written, or electronically communicated request for information relating to a specific NASD rule, SEC rule, provision of a joint industry plan (e.g., ITS, UTP, CTA, and CQA) (as promulgated and amended from time-to-time) that Nasdaq Market Operations is responsible for administering or to other duties and/or obligations imposed on Nasdaq Market Operations by the Association under the Plan of Allocation and Delegation of Function by the NASD to Subsidiaries or

otherwise; this shall include, but not be limited to, information relating to:

- (i) a clearly erroneous transaction, pursuant to NASD Rule 11890;
  - (ii) a request to reconsider a determination to withhold a primary market maker designation, pursuant to NASD Rule 4612;
  - (iii) a request for an excused withdrawal or reinstatement, pursuant to NASD Rules 4619, 4620, 4730, 5106 and 6350;
  - (iv) the resolution of a trade-through complaint, pursuant to NASD Rules 5262, 5265, and 11890;
  - (v) an ACT input error;
  - (vi) an equipment failure; or
  - (vii) a request to submit a stabilizing bid, pursuant to NASD Rules 4614 and 5106, or a request to have a quotation identified as a penalty bid on Nasdaq, pursuant to NASD Rule 4624.
- (2) A failure to comply in a timely, truthful, and/or complete manner with a request for information made pursuant to this rule may be deemed conduct inconsistent with just and equitable principles of trade.

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

In the NASD's filing with the Commission, Nasdaq included statements concerning the purpose of, and statutory basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The test of these statements may be examined at the places specified in Item IV below. Nasdaq 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

#### 1. Background

Under SEC Rule 11Ac1-1(c)(5) ("ECN Rule"),<sup>5</sup> Nasdaq market maker must reflect in its public quotes any superior prices for those orders that the market maker privately places within an ECN. The ECN Rule provides an alternative to this requirement referred to as the "ECN Display Alternative." Under the ECN Display Alternative, a market maker will be deemed to have complied with the ECN Rule if the ECN in which the market maker has placed a superior priced order has: established a link to Nasdaq by displaying the best ECN prices in Nasdaq's quote montage; and

provided non-subscribers access, through Nasdaq, to such publicly displayed prices. To accommodate the alternative, Nasdaq created the "SelectNet Linkage" which allows: (1) ECNs to display their best prices from market makers and other ECN subscribers in the Nasdaq quote montage, including the inside market display; and (2) Nasdaq member firms to access those prices by sending orders to an ECN through SelectNet. Subsequent to the implementation of the ECN Rule, the following issues have come to the attention of the Association, which have necessitated amending NASD Rules 4613(e) and 4623 and promulgating NASD Rule 4625.<sup>6</sup>

#### 2. Reserved Size

Nasdaq is proposing amendments to NASD Rule 4623 to establish the manner in which orders having a reserved size that are entered into an ECN must interact with SelectNet orders. Since ECNs have been integrated into the Nasdaq market, Nasdaq has observed that ECNs cause a percentage of locked and crossed markets.<sup>7</sup> Frequently, locks or crosses are caused by an ECN's use of "reserved" size. Specifically, an ECN may publicly display one size of an order (e.g. 1,000 shares), while maintaining a significantly larger size of the order in reserve (e.g., 10,000 shares) that is not displayed until the displayed size is executed against, that is, every time a 1,000 share order is executed against the ECN, the ECN displays another 1,000 shares at the same price until the full size of the order is exhausted. The market maker, however, does not know how many 1,000 share orders it must send to exhaust the ECN's size and take out its quote. As a result, a market maker often will send an ECN multiple SelectNet orders for the displayed size in an attempt to take the quote out. If this practice fails to take out the ECN quote, a market maker will then often

send another order for a size larger than the ECN's displayed size to try to take out not only the displayed order but also any undisplayed reserved size. Generally, however, ECNs execute SelectNet orders only for the displayed size (i.e., the market maker can only execute 1,000 shares at a time, not the full 10,000 share order.<sup>8</sup> A market maker will, after making these efforts to take out the ECN quote, post the quote it had originally wanted to post, which often results in market maker and ECN quotations locking or crossing.<sup>9</sup>

Nasdaq believes that this is inappropriate for several reasons. First, an ECN's unwillingness to execute against an order to the full extent of the ECN's reserved size may violate the best execution duty<sup>10</sup> of the broker/dealer that is operating the ECN. Specifically, Nasdaq believes that the broker/dealer sponsoring the ECN may not be complying fully with best execution obligations if that broker/dealer fills the order in small pieces at the displayed size rather than accepting an order that would fill a customer's entire order. This type of piecemeal execution is also economically inefficient and may cause customers to incur unnecessary transaction costs because multiple executions are required to fill the customer's order in full. Additionally, this type of piecemeal execution contributes to locking and crossing problems in Nasdaq, and thus has a negative impact on market quality and the maintenance of orderly markets.

Accordingly, Nasdaq is proposing an amendment to NASD Rule 4623. Under the proposal, if an ECN displays in Nasdaq an order having a reserved size and a market participant attempts to access the ECN's Nasdaq-displayed order by sending (via a Nasdaq-provided means) an order that is larger than the ECN's Nasdaq-displayed size, the ECN

<sup>8</sup> Nasdaq has noted that ECNs have the capability to accept, and from time to time will accept, SelectNet orders for more than the displayed size. Telephone Conversation between Gail Marshall-Smith, Special Counsel, Division, SEC and John F. Malitzis, Senior Attorney, Nasdaq, on July 14, 1998.

<sup>9</sup> Market makers and ECNs are required to use reasonable means not to lock or cross the market. The NASD has interpreted "reasonable means" to include preferencing a SelectNet order to the firms(s) at the bid or offer. See NASD Notice to Members 97-49. See also Letter to Joseph R. Hardiman, President, NASD, for Richard R. Lindsey, Director, Division of Market Regulation, SEC, dated November 22, 1996 (noting that, in the OTC market, a Nasdaq market maker holding a limit order that is marketable against another market maker's or ECN's quote may send a SelectNet message to the market maker or ECN displaying the existing quote. However, after using reasonable efforts to execute against the existing quote, the market maker should display the limit order even if it locks the market).

<sup>10</sup> See NASD rule 4613(b).

<sup>5</sup> The ECN Rule is embodied in SEC Rule 11Ac1-1 ("Firm Quote Rule"). See 17 CFR 240.11Ac1-1.

<sup>6</sup> Each ECN that chooses to link to Nasdaq must sign a contract that imposes certain obligations on the ECN. Among the requirements are: (1) immediate display of orders; (2) rapid and non-discriminatory execution of SelectNet orders that seek to access the ECN's quotation; and (3) provision of system description regarding the operation of the ECN. While in the past the use of contracts has worked successfully in establishing basic standards for ECN operation and activity, as the number of ECNs has increased since January 1997 it is less efficient to attempt to fashion changes to the contract to address the issues described in this filing. Nasdaq has determined that it is appropriate to propose changes to the rules governing ECNs to address uniformly, across all ECNs, the issues described in this filing.

<sup>7</sup> A locked market occurs when the quoted bid price is the same as the quoted ask price. A crossed market occurs when the quoted bid price is greater than the quoted ask price.

would be required to execute the Nasdaq-delivered order: (1) up to the size of the Nasdaq-delivered order, if the ECN order (including the reserved size and displayed portions) is the same size as or larger than the Nasdaq-delivered order; or (2) up to the size of the ECN order (including the reserved size and displayed portions), if the Nasdaq-delivered order is the same size as or larger than the ECN order (including the reserved size and displayed portions).

### 3. Locked/Crossed Markets

Nasdaq also is proposing to amend the NASD's rule governing locked and crossed markets, NASD Rule 4613(e). Nasdaq has observed instances of market makers and ECNs entering orders at 9:29 a.m. (prior to the opening when quotes are not firm) that lock or cross the market and then leaving these orders in place at 9:30 a.m. when the market opens and quotes become firm. This effectively locks/crosses the market on the opening and, therefore, disrupts the market's opening.

Although NASD Rule 4613(e) addresses the responsibility to avoid locking and crossing the market during normal business hours, the rule currently does not specifically set out the responsibility to avoid entering and leaving in place quotations that lock or cross the market on open (although Nasdaq believes that it is clear that such activity is contrary to the rule).<sup>11</sup> Accordingly, the NASD and Nasdaq are proposing to amend NASD Rule 4613(e) to clarify that if a market maker or ECN enters, at or after 9:25:00 a.m. Eastern Time, a quotation that locks or crosses the market on the opening, that market maker or ECN has an obligation to take action to avoid locking or crossing the market immediately at the market's open, but in no case later than 30 seconds thereafter (i.e., 9:30:30 a.m.). By including the 9:25 a.m. benchmark, market makers and ECNs will be better able to determine which party entered a market-locking/crossing quotation, and thus which party has the obligation to execute a transaction against a quote to unlock/uncross the market at the opening. The rule further provides that it is the responsibility of the market maker or ECN that entered the locking or crossing quotation at or after 9:25 a.m. to take action (such as sending a SelectNet order to takeout the quotation that will be crossed or locked or taking down its own quotation) to unlock/uncross the market immediately at the

open, but in no case later than 9:30:30 a.m. The 30 second period should give a market participant ample time to send a SelectNet message to the party that it locked or crossed or to take down its quote. Additionally, this provision establishes a standard by when the market participant must resolve the locked/crossed market situation—9:30:30 a.m.

Although Nasdaq believes that market participants should always monitor their preopening quotes to ensure that they do not lock/cross the market on the opening, the proposed rule includes a specific time designation of when market participants should begin monitoring their quotes, an allocation of which party is responsible for unlocking/uncrossing the market, and a specific time designation of when the locking/crossing quote must be removed. Without such standards, there could be confusion as to which quote caused the lock/cross and who has the affirmative obligation to unlock/uncross the market.

### 4. Staff Information Requests

Nasdaq also is proposing NASD Rule 4625 regarding a member's obligation to supply Nasdaq staff with certain information upon request. Nasdaq's MarketWatch and Market Operations departments have day-to-day responsibilities for administering various NASD and SEC rules, as well as for carrying out duties delegated to them by the Association. For example, Nasdaq's MarketWatch Department is responsible for, among other things, initiating trading halts and monitoring locked and crossed market situations, while Nasdaq's Market Operations Department is responsible for, among other things, reviewing ITS trade-through complaints, clearly erroneous transactions, and requests for excused withdrawals and reinstatements from unexecuted withdrawals.

In order to properly rule or to carry out a departmental function, Nasdaq staff often must obtain information on a real-time basis from a market participant. For example, when monitoring for locked and crossed markets, Nasdaq Market Watch routinely will contact the parties to the lock or cross (e.g., a market maker and/or ECN) to request relevant information.<sup>12</sup> Staff then will review this information on a real-time basis and

assist in resolving the locked or crossed market situation.<sup>13</sup>

While Nasdaq staff must request information to properly carry out its duties and responsibilities, currently there is no explicit authority in the NASD's rules that allows Nasdaq staff to do so or that requires members to comply with such requests.<sup>14</sup> While in the past, members generally have cooperated with Nasdaq staff and voluntarily provided requested information, recently some members have refused to comply with such requests. The inability to obtain necessary information frustrates the Nasdaq staff's ability to properly administer NASD and SEC rules and frustrates Nasdaq's responsibility of maintaining fair and orderly markets.

To remedy this situation, Nasdaq is proposing the adoption of NASD Rule 4625. This rule will authorize Nasdaq staff to request information in specific circumstances and will obligate members to comply with such requests. Specifically, under NASD Rule 4625 Nasdaq staff would be permitted to request from a member information directly related: to an SEC or NASD rule that the Nasdaq department is responsible for administering; or to other duties/responsibilities imposed on the Nasdaq department by the Plan of Allocation and Delegation of Function or otherwise delegated by the Associated to such department. The rule also states that the failure to provide information could subject the member to a disciplinary action.

### 5. Statutory Basis

Nasdaq believes that the proposed rule changes are consistent with Sections 15A(b)(6), 15A(b)(11), and 11A(a)(1)(C) of the Act. Among other things, Section 15A(b)(6) requires that the rules of a national securities association be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation

<sup>13</sup> In addition to the locks and crosses, there are other instances when staff must gather information from market makers and ECNs on a real-time basis. For example, Nasdaq Market Watch may need to contact a market maker or ECN to determine quickly if a trade, quotation, or series of trades appearing to be aberrations, were caused by a malfunction of a computer system (which could pose a threat to the integrity of Nasdaq from a technological perspective) or by some other source.

<sup>14</sup> While staff of NASD Regulation currently has authority under Rule 8210 to request information from members, such authority may be exercised only in connection with a current investigation, filed complaint, examination, or authorized disciplinary proceeding. Nasdaq staff requests information to administer a rule, and does not request information in connection with a filed complaint.

<sup>11</sup> Nasdaq has previously noted that it is especially important at the opening that members monitor their quotes as well as any orders placed in ECNs to avoid locking or crossing the market during the opening. See Notice to Members 97-49.

<sup>12</sup> Staff may request information on the identity of the customers, trade information, the reason for the lock or cross (e.g., system error), and other information related to the locked or crossed market situation.

and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to an perfect the mechanisms of a free and open market and a national market system and in general to protect investors and the public interest.<sup>15</sup> Section 15A(b)(11) empowers the NASD to adopt rules governing the form and content of quotations relating to securities in the Nasdaq market.<sup>16</sup> Such rules must be designed to produce fair and informative quotations, prevent fictitious or misleading quotations, and promote orderly procedures for collecting, distributing, and publishing quotations. Section 11A(a)(1)(C) provides that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to, among other things, assure the economically efficient execution of securities transactions and the availability to brokers, dealers, and investors of information with respect to quotations for and transactions in securities, and to assure fair competition among brokers and dealers.<sup>17</sup>

Specifically, the reserved size proposal is consistent with Sections 11A(a)(1)(C) and 15A(b)(6). This proposal helps to ensure that members meet their best execution obligations and discourages piecemeal executions, which may be economically inefficient and costly to the customer. Thus, the proposal promotes just and equitable principles of trade and the protection of investors and the public interest. Additionally, the rule helps remove impediments to and perfect the mechanism of a free and open market, and ensures economically efficient executions by discouraging piecemeal executions of large orders.

The proposal to require members to provide Nasdaq staff with information and the amendments to NASD Rule 4613(e) are consistent with Sections 15A(b)(6) and 11A(a)(1)(C). By requiring market makers and ECNs to avoid locks and crosses on the market's opening and to provide Nasdaq staff with information necessary to administer NASD and SEC rules, these proposed rules foster cooperation and coordination with members. These two proposals also ensure the fair and orderly operation of Nasdaq, as they clearly delineate the obligations regarding the entry of quotations that lock/cross the market at the opening and permit staff to gather information

necessary to administer particular rules or to discharge particular departmental duties.

#### *B. Self-Regulatory Organization's Statement on Burden on Competition*

Nasdaq 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.

#### *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 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. Solicitations of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. 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 file number SR-NASD-98-01 and should be submitted by August 14, 1998.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>18</sup>

**Jonathan G. Katz,**

Secretary.

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-40224; File No. SR-NSCC-98-2]

### **Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change Allowing Users of NSCC's Mutual Fund Services ("MFS") Access to Annuity Processing Services ("APS") and to Allow Users of APS Access to MFS**

July 16, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on March 12, 1998, the National Securities Clearing Corporation ("NSCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change and on March 26, 1998, amended the proposed rule change as described in Items I and II below, which items have been prepared primarily by NSCC. The Commission is publishing this notice and order to solicit comments from interested persons and to grant accelerated approval of the proposed rule change.

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

The proposed rule change amends NSCC's rules to allow users of NSCC's Mutual Fund Services ("MFS") access to Annuity Processing Services ("APS") and to allow users of APS access to MFS.

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

In its filing with the Commission, NSCC 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. NSCC has prepared summaries, set forth in sections (A), (B),

<sup>15</sup> 15 U.S.C. 78o-3(b)(6).

<sup>16</sup> 15 U.S.C. 78o-3(b)(11).

<sup>17</sup> 15 U.S.C. 78k-1(a)(1)(C).

<sup>18</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).