

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 the filing will also be available for inspection and copying at the principal offices of the Board. All submissions should refer to File No. SR-MSRB-00-01 and should be submitted by March 2, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-42381; File No. SR-NYSE-99-25]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. Relating to Amendments to Exchange Rule 134, Governing Error Accounts, and New Rule 407A, Concerning Floor Member Account Disclosure

February 3, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June 15, 1999, the New York Stock Exchange, Inc. ("NYSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, III below, which Items have been prepared by the Exchange. On December 13, 1999, the NYSE filed Amendment No. 1 to the proposed rule change with the Commission.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change as amended from interested persons.

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

The proposed rule change consists of amendments to existing rules governing error accounts (Rule 134) and a new rule regarding Floor member account disclosure (Rule 407A).

#### 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 Exchange 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 Exchange 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. Purpose

The Exchange is proposing a series of initiatives to strengthen the regulation of activities of members on the Floor. The initiatives proposed herein consist of amendments to existing rules governing error accounts and a new rule regarding Floor member account disclosure.<sup>4</sup>

*Error Accounts.* The Exchange is proposing to revise NYSE Rule 134(d) to require that each member maintain an error account. Under the proposed rule change, if a member does not maintain an error account, he or she will not be permitted to transact business on the Floor. Only one error account will be permitted for each member. The error account may be maintained in the member's name or in the name of his or her member organization, or the member may participate in an error account established for a group of members.

At present there is no requirement that a member maintain an error account. The Exchange believes that the amendment to Rule 134 will enhance its ability to monitor and detect potential abuses such as on-Floor trading by members. Error account transaction information will be localized to one place for each member, and not scattered among several accounts which, at present, could be held in the name of another member or member organization.

*Housing Error Accounts.* The proposed rule change, as amended,

would require that a member's error account be maintained at a broker or dealer registered in accordance with Section 15(b)<sup>5</sup> of the Act. The Exchange believes that this provision would enable it to use its oversight authority to review error records for the brokers or dealers which are members or member organizations of the Exchange. If the error account is maintained at a non-member broker or dealer, the Exchange represents that it will work through the Intermarket Surveillance Group ("ISG") to obtain information on errors. The Exchange believes this requirement is necessary to enable review of situations involving errors in an expedited fashion.

*Error Transaction Procedures.* The proposed rule change would require that if a member or member organization acquires or assumes a security position resulting from an error transaction, or initiates a transaction to offset an error transaction, such transaction must be recorded and cleared in the member's or his or her member organization's error account, or in an error account established for a group of members.

This would include situations where the execution was wrong (e.g., wrong side of the market, wrong stock) and where the member "missed the market" by failing to execute the order in the prevailing market. If the error can be corrected at a better price at the time the error is discovered, the better price must be offered to the customer. If the customer refuses the superior execution, a record of this must be maintained by the member.

Alternatively, a customer could accept the error, in which case the transaction would be placed in the customer's account. An error transaction could also be accepted by the specialist in the security into his or her organization's account as a trade "on account of error."

When a customer accepts an error transaction, a monetary settlement (a "difference check") may be made by the member or member organization. If the difference check is for more than \$500, the member or member organization involved would be required under the proposal to maintain records detailing the transaction. In some instances, a customer may accept an error, but not wish to receive a difference check for bookkeeping or other reasons. The member or member organization involved would be required to maintain records in these situations, as well.

The proposal further prescribes the way a member would be required to

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

<sup>13</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> The substance of Amendment No. 1 is incorporated into this notice.

<sup>4</sup> See Exchange Act Release No. 41706 (August 4, 1999), 64 FR 44069 (August 12, 1999) (File No. SR-NYSE-98-25) relating to proposed adoption by the NYSE of new provisions for recording the details of an order in an electronic system prior to representing or executing an order on the Floor. The two rule changes proposed in this filing replace the equivalent proposals that were deleted by amendment from SR-NYSE-98-25. See note 4, *id.*

<sup>5</sup> 15 U.S.C. 78o(b).

handle an error that is not accepted by a customer. Where the member is representing an order that cannot be executed pursuant to its term,<sup>6</sup> the member would be required to issue an execution report covering the customer's order at the missed market price from his or her error account, the member organization's error account or the specialist's account if the specialist agreed to take in the error. The member would be permitted to confirm such report as an Exchange transaction as long as the position in the error account or specialist's account is liquidated.

The Exchange stipulates that if the order can be executed on its original terms or on better terms, the member or member organization is expected to execute the order pursuant to its terms, as would typically be the case with a "not held" order. A member representing a "not held" order is not permitted to "miss the market." and must execute the order pursuant to its terms. The member would not be permitted to simply issue a report out of his or her error account.

**Recordkeeping.** The proposed rule change would require the member of his or her member organization to maintain records with respect to all errors. These records would include the audit trail data elements prescribed in NYSE Rule 132, as well as the nature and amount of error, how the member resolved the error with the member or member organization, including a specialist, which cleared the error trade on the member's behalf, and the aggregate amount of liability that the member has incurred and has outstanding as of the time the error is recorded. The Exchange could also require that additional data elements be recorded in circumstances where the Exchange believe that such additional information is necessary for all error transactions, or in particular situations. The Exchange believes that the recordkeeping requirement would enable the Exchange to review and analyze error transactions on a current and consistent basis.

**Profitable Errors.** The Proposal would also establish reporting requirements with respect to certain "profitable" errors. These are errors which can be liquidated at a price that is favorable to the position acquired in the member or member organization's error account. Under the proposal, every member not associated with a member organization and every member associated with a member organization that derives at

least 75% of its revenue from floor brokerage would be required to report to the Exchange error transactions that result in a profit of more than \$500 for any transaction or more than \$3,000 in any calendar week. The Exchange believes this will enable it to quickly review these situations for possible violations of Floor Trading rules or procedures.

The Exchange notes that all members and member organizations would be required under the proposal to maintain details of all errors, profitable or not. For members and member organizations that do not act primarily as a Floor broker, these records would be reviewed in connection with the normal oversight activities of the Exchange.

**Reports of Closed Error Accounts.** The proposed rule change would also require each clearing member organization to report to the Exchange whenever it ceases to carry an error account. The notice would be required in writing immediately, but no later than the opening of the Exchange on the following business day.

**Member Account Disclosure.** Proposed new Rule 407A would provide the Exchange with information on accounts of members. The provision would require a member to report to the Exchange any securities account in which the member has a direct or indirect financial interest or over which the member has discretionary authority. This would include any account at a non-member broker-dealer, investment adviser, bank or other financial institution. In addition, the member would be required to notify the financial institution that carries or services his or her account or an account over which the member has discretionary authority that he or she is a member of the Exchange.

Purchases of securities of a publicly-traded registered investment company directly from the issuer or principal underwriter would not be considered a reportable securities account. However, interests in a non-publicly-traded investment vehicle, including hedge funds, would be reportable.

The Exchange believes that these reporting requirements would provide it with current information on where members carry securities accounts and enhance its ability to investigate quickly the trading of securities by members of the Exchange.

## 2. Statutory Basis

The Exchange bases the proposed rule change on Section 6(b)(5)<sup>7</sup> of the Act, which requires that an exchange have

rules that are designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The Exchange believes that the proposed rule change will help accomplish these ends by strengthening the Exchange's ability to surveil the Floor activities of members.

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

The Exchange does not believe that the proposed rule change will impose 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*

The Exchange has neither solicited nor received written comments on 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) 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 Exchange 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, 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. 20549-0609. 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

<sup>6</sup> An example of such an order is a "held" order to buy with a limit of 20, which cannot be executed pursuant to its terms if the member missed the market and the stock is now trading above 20.

<sup>7</sup> 15 U.S.C. 78f(b)(5).

the Commission's Public Reference Room. Copies of the filing will also be available for inspection and copying at the principal offices of the Exchange. All submissions should refer to File No. SR-NYSE-99-25 and should be submitted by March 2, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-42384; File No. SR-PCX-99-10]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Pacific Exchange, Inc. Amending Its Disciplinary Procedures

February 3, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("ACT")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on April 2, 1999, the Pacific Exchange, Inc. ("PCX" 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 PCX. On June 25, 1999, the PCX filed with the Commission Amendment No. 1 to the proposed rule change.<sup>3</sup> On January 18, 2000, the PCX filed with the Commission Amendment No. 2 to the proposed rule change.<sup>4</sup> On January 19, 2000, the PCX filed with the Commission Amendment No. 3 to the proposed rule change.<sup>5</sup> The Commission

is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The PCX is proposing to amend its rules on disciplinary proceedings at the Exchange,<sup>6</sup> and in particular, to add new rules to codify the independent function of PCX Regulatory Staff; to clarify what communications are improper in the context of pending investigations or disciplinary proceedings; to provide PCX Regulatory Staff with the ability to issue formal complaints for the alleged violation of Exchange rules; to permit qualified persons who are not members to serve on hearing panels; and otherwise to codify procedures relating to hearing panelists' conflicts of interest. Below is the text of the proposed rule change. Proposed new language is in *italics*; proposed deletions are in [brackets].

\* \* \* \* \*

#### Rule 10

##### Disciplinary Jurisdiction and Appeals

###### ¶6061 Disciplinary Jurisdiction

Rule 10.1—No change.

###### ¶6067 Investigations and Regulatory Cooperation

Rule 10.2(a). The Exchange *Regulatory Staff will function independently of the commercial interests of the Exchange members and will have the sole discretion to investigate, and will [shall] investigate,* possible violations within the disciplinary jurisdiction of the Exchange. [upon order of the Board of Governors, the Executive Committee, the Ethics and Business Conduct Committee, or the Floor Trading Committees or upon receipt of a complaint alleging such violations filed by a member or by any other person.] *No member of the Board of Governors or the Executive Committee or non-Regulatory Staff may interfere with or attempt to influence the process or resolution of any pending investigation or disciplinary proceeding.* [All such complaints should specify in reasonable detail the facts constituting the violation, including the specific statutes, Exchange Constitutional provisions, Rules, commentaries, resolutions, policies or procedures allegedly violated. A member or person

associated with a member is entitled to be represented by counsel during any Exchange investigation.

(b) No member or person associated with a member shall impede or delay an Exchange investigation with respect to possible violations within the disciplinary jurisdiction of the Exchange nor refuse to furnish testimony, documentary materials or other information requested by the Exchange during the course of its investigation. Failure to furnish such testimony, documentary materials or other information requested by the Exchange pursuant to this Rule on the date or within the time period required by the Exchange shall be considered obstructive of an Exchange inquiry or investigation and subject to formal disciplinary action.]

(b) *Any person, any Exchange committee, the Board of Governors or the Executive Committee may submit for investigation a complaint alleging possible violations. Each complaint must specify in reasonable detail the facts constituting the violation and any specific federal statute, rule, regulation or Exchange constitutional provision, rule, commentary, resolution, policy or procedure allegedly violated.*

[(c) A member or member organization shall submit such trade data elements specified in Commentary .01 below in such automated format as may be prescribed by the Exchange from time to time, in regard to such transaction or transactions as may be the subject of a particular request for information made by the Exchange. Failure to submit such data in the required format shall be considered obstructive of an Exchange inquiry or investigation and subject to formal disciplinary action.]

(c) *A member, member organization or associated person is entitled to be represented by counsel during any Exchange investigation.*

[(b)] (d) No member, member organization, [or person associated with a member] *associated person or other person or entity over whom the Exchange has jurisdiction pursuant to Rule 10.1(b) may [shall] impede or delay an Exchange investigation with respect to possible violations within the disciplinary jurisdiction of the Exchange nor refuse to furnish testimony, documentary materials or other information requested by the Exchange during the course of its investigation. Failure to furnish such testimony, documentary materials or other information requested by the Exchange pursuant to this Rule on the date or within the time period required by the Exchange [shall] will be*

<sup>8</sup> 17 CFR 200.3-3(a)(12).

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

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See letter from Michael D. Pierson, Director, Regulatory Policy, PCX, to Michael A. Walinskas, Associate Director, Division of Market Regulation, Commission, dated June 24, 1999 ("Amendment No. 1"). In Amendment No. 1, the Exchange withdrew proposed PCX Rule 10.8, *Hearing Panels*, and renumbered two of the proposed rules.

<sup>4</sup> See letter from Michael D. Pierson, Director, Regulatory Policy, PCX, to Jennifer Colihan, Attorney, Division of Market Regulation, Commission, dated January 7, 2000 ("Amendment No. 2"). In Amendment No. 2, the Exchange proposed to delete PCX Rule 10.4(f) among other things.

<sup>5</sup> See letter from Michael D. Pierson, Director, Regulatory Policy, PCX, to Kelly Riley, Attorney, Division of Market Regulation, Commission, dated January 14, 2000 ("Amendment No. 3"). In Amendment No. 3, the Exchange proposed to make minor word change and change the heading for proposed Rule 10.4(c) from "Summary Proceedings" to "Summary Determinations" among other things.

<sup>6</sup> The Commission notes that the Exchange has proposed a similar disciplinary structure and procedures for the Pacific Equities, Inc. See Exchange Act Release No. 42178 (Nov. 24, 1999) 64 FR 68136 (Dec. 6, 1999) (File No. SR-PCX-99-39).