

Option class	Market-maker surcharge (per contract)	Order book official brokerage rate (per contract) <sup>5</sup>
The Boeing Company (BA) .....	0.14	\$0.00
Friede Goldman International (FGI) .....	0.02	0.00
Northwest Airlines Corporation (NAQ) .....	0.02	0.00
Open Market, Inc. (OQM) .....	0.02	0.00
Orbital Science Corp. (ORB) .....	0.02	0.00
Onsale, Inc. (QOL) .....	0.02	0.00
Prime Medical Services, Inc. (QSI) .....	0.02	0.00
Synovous Financial Corp. (SNV) .....	0.02	0.00
Wackenhut Corrections Corp. (WHC) .....	0.02	0.00
Zebra Technologies Corp. (ZBQ) .....	0.02	0.02

<sup>5</sup> The market-maker surcharge will be used to reimburse the Exchange for the reduction in the OBO brokerage rate from \$0.20 in the relevant option classes. Any remaining funds will be paid to SFBs as provided in Exchange Rule 2.40.

These fees went into effect on Thursday, September 2, 1999. All of the option classes above are currently multiple listed on at least one other exchange. The most recent certification for multiple listing relates to options on The Boeing Company (BA) ("Boeing"), which were listed on the Pacific Exchange ("PCX") beginning on September 2, 1999. All of the market-maker surcharge fees, except those applicable to Boeing, reflect reductions in former market-maker surcharge fees imposed pursuant to Exchange Rule 2.40.

With respect to options on Boeing, CBOE Rule 2.40(e) requires that an option be listed for trading on another exchange before a market-maker surcharge fee can be assessed. Boeing has been certified by the Options Clearing Corporation to be listed on the PCX. Therefore, the CBOE began assessing the market-maker surcharge on September 2, 1999, when Boeing was first listed on the PCX.<sup>6</sup>

The CBOE represents that the market-maker surcharge fees were effective from September 2, 1999 until the options at issue were designated to DPMs—September 7, 1999 for FGI, NAQ, OQM, QOL, QSI, SNV, WHC, and ZBQ, and September 13, 1999 for BA. The fees were eliminated when the options were designated to DPMs.<sup>7</sup>

## 2. Statutory Basis

The proposed rule change is consistent with Section 6(b) of the Act,<sup>8</sup> in general, and furthers the objectives of

<sup>6</sup> The Exchange interprets Rule 2.40 to allow the EFPC to vote on market-maker surcharge before a class has been listed for trading on another exchange. Rule 2.40, however, provides that the market-maker surcharge may not actually be assessed until the class has been listed for trading on another exchange.

<sup>7</sup> Telephone conversation between Stephanie C. Mullins, Attorney, CBOE, and Gordon Fuller, Special Counsel, Division, Commission (December 10, 1999).

<sup>8</sup> 15 U.S.C. 78f(b).

Section 6(b)(4),<sup>9</sup> in particular, in that it is designed to provide for the equitable allocation of reasonable dues, fees, and other charges among CBOE 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 not necessary or appropriate in furtherance of the purposes of the Act.

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

The Exchange did not solicit or receive written comments on the proposed rule change.

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

Because the foregoing rule change establishes or changes a due, fee, or other charge imposed by the Exchange, it has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act,<sup>10</sup> and Rule 19b-4(f)(2)<sup>11</sup> thereunder. At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.<sup>12</sup>

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule

<sup>9</sup> 15 U.S.C. 78f(b)(4).

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>11</sup> 15 CFR 240.19b-4(f)(2).

<sup>12</sup> In reviewing this proposal, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

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, NW., Washington, DC 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 the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the CBOE. All submissions should refer to the File No. SR-CBOE-99-52 and should be submitted by March 2, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-42385; File No. SR-MSRB-00-01]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Supervision of Correspondence With the Public

February 3, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934

<sup>13</sup> 17 CFR 200.30-3(a)(12).

("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on January 7, 2000, the Municipal Securities Rulemaking Board ("Board" or "MSRB") 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 Board. 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 Board has filed proposed amendments to MSRB Rules G-8, on books and records, G-9, on record retention, and G-27, on supervision (hereinafter referred to as the "proposed rule change"). The proposed rule change will revise the Board's supervision and record retention rules to provide dealers with flexibility in developing reasonable procedures for the review of correspondence with the public. The amendments are intended to recognize the growing use of correspondence sent and received in electronic format while still providing for effective supervision. The Board has also filed with the Commission a draft notice that will provide guidance to dealers on how to implement these rule changes. The proposed rule change and accompanying notice are modeled after and designed to conform to the rules and guidance of the National Association of Securities Dealers ("NASD"). The text of the proposed rule change is set forth below. Additional are italicized and deletions are bracketed.

\* \* \* \* \*

#### Rule G-8: Books and Records to be made by Brokers, Dealers and Municipal Securities Dealers

(a) Description of Books and Records Required to be Made. Except as otherwise specifically indicated in this rule, every broker, dealer and municipal securities dealer shall make and keep current the following books and records, to the extent applicable to the business of such broker, dealer or municipal securities dealer:

(i)-(xix) No Change.

(xx) *Records Concerning Compliance with Rule G-27. Each broker, dealer and municipal securities dealer shall maintain the records required under G-27(c) and G-27(d).*

(b)-(f) No Change.

#### Rule G-: Preservation of Records

(a) No Change.

(b) Records to be Preserved for Three Years. Every broker, dealer and municipal

securities dealer shall preserve the following records for a period of not less than three years:

(i)-(vii) No Change.

(viii) the following records, to the extent made or received by such broker, dealer or municipal securities dealer in connection with its business as such broker, dealer or municipal securities dealer and not otherwise described in this rule:

(A)-(B) No Change.

(C) all written and electronic communications received and sent, including inter-office memoranda, relating to the conduct of the activities of such broker, dealer or municipal securities dealer with respect to municipal securities;

(D)-(E) No Change.

(ix)-(xiii) No Change.

(xiv) *the records to be maintained pursuant to Rule G-8(a)(xx).*

#### Rule G-27: Supervision

(a)-(b) No change

(c) Written supervisory procedures. Each dealer shall adopt, maintain and enforce written supervisory procedures reasonably designed to ensure that the conduct of the municipal securities activities of the dealer and its associated persons are in compliance as required in section (a) of this rule. Such procedures shall codify the dealer's supervisory system for ensuring compliance and, at a minimum, shall establish procedures

(i)-(vi) No change

(vii) for the prompt review and written approval by a designated principal of:

(A) the opening of each customer account introduced or carried by the dealer in which transactions in municipal securities may be effected; and

(B) each transaction in municipal securities on a daily basis, including each transaction in municipal securities effected with or for a discretionary account introduced or carried by the dealer [; and

(C) all correspondence pertaining to the solicitation or execution of transactions in municipal securities].

(d) *Review of Correspondence*

(i) *Supervision of Municipal Securities Representatives. Each dealer shall establish procedures for the review by a designated principal of incoming and outgoing written (i.e., non-electronic) and electronic correspondence of its municipal securities representatives with the public relating to the municipal securities activities of such dealer. Such procedures must be in writing and be designed to reasonably supervise each municipal securities representative. Evidence that these supervisory procedures have been implemented and made available, upon request, to a registered securities association or the appropriate regulatory agency as defined in Section 3(a)(34) of the Act.*

(ii) *Review of correspondence. Each dealer shall develop written procedures that are appropriate to its business, size, structure, and customers for the review of incoming and outgoing written (i.e., non-electronic) and electronic correspondence with the public relating to its municipal securities activities. Procedures shall include the*

*review of incoming, written correspondence directed to municipal securities representatives and related to the dealer's municipal securities activities to properly identify and handle customer complaints and to ensure that customer funds and securities are handled in accordance with the dealer's procedures. Where such procedures for the review of correspondence do not require review of all correspondence prior to use or distribution, they must include provisions for the education and training of associated persons as to the dealer's procedures governing correspondence; documentation of such education and training; and surveillance and follow-up to ensure that such procedures are implemented and adhered to.*

(iii) *Retention of correspondence. Each dealer shall retain correspondence of municipal securities representatives relating to its municipal securities activities in accordance with rules G-8(a)(xx) and G-9(b)(viii) and (xiv). The names of the persons who prepared outgoing correspondence and who reviewed the correspondence shall be ascertainable from the retained records and the retained records shall be readily available, upon request, to a registered securities association or the appropriate regulatory agency as defined in section 3(a)(34) of the Act.*

[(d)] (e) Deputy to update and review written procedures. Each dealer shall revise and update its written supervisory procedures as necessary to respond to changes in Board or other applicable rules and as other circumstances require. In addition, each dealer shall review, at least on an annual basis, its supervisory system and written supervisory procedures adopted under sections (c) and (d) of this rule to determine whether they are adequate and up-to-date and shall ensure that the dealer is in compliance with this rule.

\* \* \* \* \*

### 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 Board 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 Board 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

##### i. Background

In May 1996, the Commission issued an Interpretive Release on the use of Electronic Media by the Broker-Dealers,

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

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

Transfer Agents, and Investment Advisors for Delivery of Information.<sup>3</sup> That release expressed the views of the Commission with respect to the delivery of information through electronic media in satisfaction of requirements in the federal securities laws, but did not address the applicability of any self-regulatory organization ("SRO") rules. In the release the Commission did, however, strongly encourage the SROs to work with broker-dealer firms to adopt SRO supervisory review requirements governing communications with customers to accommodate the use of electronic media.<sup>4</sup>

On December 31, 1997, the Commission approved proposed rule changes filed by the NASD<sup>5</sup> and New York Stock Exchange ("NYSE")<sup>6</sup> to update rules governing supervision of communication with the public. NASD Notice to Members ("NTM") 98-11 announced approval of the proposed rule change and provided implementation guidance to dealers.

Most of these rules became effective on April 7, 1998.<sup>7</sup> In response to public comment and certain Commission concerns, the NASD subsequently proposed further changes to these rules which were approved by the Commission and became effective on March 15, 1999.<sup>8</sup> NASD NTM 99-03 provided guidance on the further changes.<sup>9</sup>

As amended, NASD Rule 3010(d)(1) provides that procedures for review of correspondence with the public relating to a member's investment banking of securities business be designed to provide reasonable supervision for each registered representative, be described in an organization's written supervisory procedures, and be evidenced in an appropriate manner.

NASD Rule 3010(d)(2), as amended, requires each member to develop written policies and procedures for review of correspondence with the public relating to its investment banking or securities business tailored to its structure and the nature and size of its business and customers. These

procedures must also include the review of incoming, written correspondence directed to registered representatives and related to the member's investment banking or securities business to properly identify and handle customer complaints and to ensure that customer funds and securities are handled in accordance with dealer's procedures.

The Board has determined to adopt substantially similar rule changes. The Board believes that conforming its rule language to the language in the NASD rules will help ensure a coordinated regulatory approach to the supervision of correspondence. In addition, in connection with Commission approval of the proposed rule change, the Board will issue a notice to dealers to provide guidance to dealers on how to implement the proposed rule changes. This guidance has been coordinated with NASD NTM 98-11 and NASD NTM 99-03 and is described below.

#### ii. Description of the Rule as Revised Supervision of Municipal Securities Representatives

The proposed amendments to MSRB Rule G-27(d), provide, among other things, that a dealer must establish procedures for the review by a designated principal of each municipal securities representative's incoming and outgoing written (*i.e.*, non-electronic) and electronic correspondence with the public relating to the municipal securities activities of such dealer. The procedures must be designed to provide reasonable supervision of each municipal securities representative and must be described in the dealer's written supervisory procedures. Implementation and execution of these procedures must be clearly evidenced, and the evidence must be maintained and be made available upon request to a registered securities association or the appropriate regulatory agency as defined in section 3(a)(34)<sup>10</sup> of the Act.

#### Procedures for Review of Correspondence

Currently, MSRB Rule 27(c)(vii)(C) provides that each dealer shall establish procedures for the review and written approval by a designated principal of all correspondence pertaining to the solicitation or execution of transactions in municipal securities. Under the proposed MSRB Rule G-27(d)(ii), a review of each item of correspondence will no longer be required. Dealers will be allowed flexibility in developing procedures for the review of correspondence relating to the dealer's municipal securities activities—both

incoming and outgoing, written or electronic—tailored to the nature and size of the dealer's business and customers.

With respect to incoming, written (*i.e.*, non-electronic) correspondence directed to municipal securities representatives and related to the municipal securities activities of the dealer, the proposal would require review of the correspondence to properly identify and handle customer complaints and to ensure that customer funds and securities are handled in accordance with the dealer's procedures. The proposed rule change does not require review of all correspondence prior to use or distribution. However, any dealer that does not conduct electronic or manual pre-use review of each item of correspondence will be required to regularly educate and train its associated persons as to the dealer's procedures governing review of correspondence, document such education and training, and monitor to ensure compliance with such procedures.

#### Retention of Correspondence

The proposed rule change will include amendments to MSRB Rules G-8(a)(xx), G-9(b)(viii) and (xiv), and G-7(d)(i), (ii), and (iii) requiring each dealer to preserve correspondence of municipal securities representatives relating to the municipal securities activities and maintain the records of written supervisory procedures, education and training required under Rule G-27(c) and (d) for three years. The proposed rule change also requires that the names of the persons who prepared and reviewed correspondence must be ascertainable from the retained records and the records must be made available, upon request, to the appropriate enforcement agency (*i.e.*, NASD or federal bank regulatory agency).

#### Draft Notice-Guidelines for Supervision and Review

The notice to dealers will provide guidance on how to implement the proposed rule change. In particular, the notice states that in adopting review procedures pursuant to Rule G-27(d)(i), dealers must:

- Specify, in writing, the dealer's policies and procedures for reviewing different types of correspondence;
- Identify how supervisory reviews will be conducted and documented;
- Identify what types of correspondence will be pre- or post-reviewed;
- Identify the organizational position(s) responsible for conducting review of the different types of correspondence;

<sup>3</sup> See Securities Act Release No. 7288, Exchange Act Release No. 37182, Investment Company Act Release No. 21945, Investment Advisor Act Release No. 1562 (May 9, 1996), 61 FR 24644 (May 15, 1996) (File No. S7-13-96).

<sup>4</sup> *Id.*

<sup>5</sup> See Exchange Act Release No. 39510 (December 31, 1997), 63 FR 1131 (January 8, 1998).

<sup>6</sup> See Exchange Act Release No. 39511 (December 31, 1997), 63 FR 1135 (January 8, 1998).

<sup>7</sup> See Exchange Act Release No. 39866 (April 14, 1998), 63 FR 19778 (April 21, 1998).

<sup>8</sup> See Exchange Act Release No. 40372 (August 27, 1998), 63 FR 47059 (September 3, 1998).

<sup>9</sup> See NTM 99-03 (January 1999).

<sup>10</sup> 15 U.S.C. 78c(a)(34).

- Specify the minimum frequency of the reviews for each type of correspondence;
- Monitor the implementation of and compliance with the dealer's procedures for reviewing public correspondence; and
- Periodically re-evaluate the effectiveness of the dealer's procedures for reviewing public correspondence and consider any necessary revisions.

The notice also states that in conducting reviews, dealers may use reasonable sampling techniques. As an example of appropriate evidence of review, e-mail related to the dealer's municipal securities activities may be reviewed electronically and the evidence of review may be recorded electronically.

In developing supervisory procedures for the review of correspondence with the public pursuant to Rule G-27(d)(ii), the notice states that each dealer must consider its structure, the nature and size of its business, other pertinent characteristics, and the appropriateness of implementing uniform firm-wide procedures or tailored procedures (*i.e.*, by specific function, office/location, individual, or group of persons).

The notice also provides guidance on adopting review procedures pursuant to Rule G-27(d)(ii), and states that dealers must, at a minimum:

- Specify procedures for reviewing municipal securities representatives' recommendations to customers;
- Require supervisory review of some of each municipal securities representative's public correspondence, including recommendations to customers;
- Consider the complaint and overall disciplinary history, if any, of municipal securities representatives and other employees (with particular emphasis on complaints regarding written or oral communications with clients); and
- Consider the nature and extent of training provided municipal securities representatives and other employees, as well as their experience in using communications media (although a dealer's procedures may not eliminate or provide for minimal supervisory reviews based on an employee's training or level of experience in using communications media).

In addition, the notice provides that supervisory and procedures must also:

- Provide that all customer complaints, whether received via e-mail or in written form from the customer, are kept and maintained;
- Describe any dealer standards for the content of different types of correspondence; and
- Prohibit municipal securities representatives' and other employees' use of electronic correspondence to the public unless such communications are subject to supervisory and review procedures developed by the dealer. For example, the Board would expect dealers to prohibit correspondence with customers from

employees' home computers or through third party systems unless the dealer is capable of monitoring such communications.

The notice also states that the method used for conducting reviews of incoming, written correspondence to identify customer complaints and funds may vary depending on the dealer's office structure. Where the office structure permits review of all correspondence, dealers should designate a municipal securities representative or other appropriate person to open and review correspondence prior to use or distribution to identify customer complaints and funds. The designated person must not be supervised or under the control of the municipal securities representative whose correspondence is opened and reviewed. Unregistered persons who have received sufficient training to enable them to identify complaints and funds would be permitted to review correspondence.

Where the office structure does not permit the review of correspondence<sup>11</sup> prior to use or distribution, appropriate procedures that could be adopted include the following:

- Forwarding opened incoming, written correspondence related to the dealer's municipal securities activities to a designated office, or supervising branch office, for review on a weekly basis;
- Maintenance of a separate log for all checks received and securities products sold, which is forwarded to the supervising branch office on a weekly basis;
- Communication to clients that they can contact the dealer directly for any matter, including the filing of a complaint, and providing them with an address and telephone number of a central office of the dealer for this purpose; and
- Branch examination verification that the procedures are being followed.

## 2. Statutory Basis

The Board believes that the proposed rule change is consistent with Section 15B(b)(2)(C)<sup>12</sup> of the Act, which requires, in pertinent part, that the Board's rules shall:

be 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 regulating, clearing, settling, processing information with respect to, and facilitating transactions in municipal securities, to remove impediments to and perfect the mechanism of a free and open market in municipal securities, and, in general, to protect investors and the public interest.

<sup>11</sup> Amended language per telephone conversation between Carolyn Walsh, Assistant General Counsel, MSRB, and Ira L. Brandriss, the Commission, February 3, 2000.

<sup>12</sup> 15 U.S.C. 78o-4(b)(2)(c).

In particular, the Board believes that the proposed rule change is consistent with the Act in allowing dealers to use new technology, such as e-mail and the Internet, while still providing for appropriate supervision and review. In addition, the proposed rule change will make the Board's rules on supervision and record retention substantially similar to the NASD rules. The Board believes that such similar rules by the self-regulatory organizations should facilitate dealer compliance with these requirements.

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

The Board does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in the furtherance of the Act's purposes because it would apply equally to all brokers, dealers and municipal securities dealers.

## 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 **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 Board 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 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.*

[FR Doc. 00-3038 Filed 2-9-00; 8:45am]

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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).