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 on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange neither solicited nor received written comments with respect to the proposed rule change.

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

This proposed rule filing has been filed by the Exchange as a ''non-controversial'' rule change pursuant to Section 19(b)(3)(A) of the Act [10] and subparagraph (f)(6) of Rule 19b–4 thereunder.[11] Because the foregoing proposed rule change: (1) Does not significantly affect the protection of investors or the public interest, (2) does not impose any significant burden on competition, (3) by its terms does not become operative for 30 days after the date of filing, or such shorter time as the Commission may designate, and (4) the Commission is waiving the required written notice of intent to file the proposed rule change at least five days prior to the filing date, it has become effective pursuant to Section 19(b)(3)(A) of the Act [12] and Rule 19b–4(f)(6) thereunder.[13]

The Commission has determined, consistent with the protection of investors and the public interest, to make the proposed rule change operative upon filing, pursuant to Section 19(b)(3)(A) of the Act and Rule 19b–4(f)(6)(iii).[14] Under Rule 19b–4(f)(6)(iii), a proposed ''non-controversial'' rule change does not become operative for 30 days after the date of filing, unless the Commission designates a shorter time.[15] The Commission believes that it is consistent with the protection of investors and the public interest to make the proposed rule change operative upon filing because: (1) Members were notified in October that the Exchange would propose that the electronic filing requirement become effective beginning with the filing of the January 2000 FOCUS Reports, (2) the Exchange provided the necessary software for electronic filing, and (3) the purpose of the electronic filing requirement is to facilitate the filing process for members.

At any time within 60 days of the filing of the amended proposed rule change, the Commission may summarily abrogate such rule 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.[16]

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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 amended 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 also will be available for inspection and copying at the principal office of the CHX. All submissions should refer to File No. SR–CHX–00–01 and should be submitted by March 23, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[17]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00–5062 Filed 3–1–00; 8:45 am]

BILLING CODE 8010–01–M

[10] 15 U.S.C. 78s(b)(3)(A).

[11] 17 CFR 240.19b–4(f)(6).

[12] 15 U.S.C. 78s(b)(3)(A).

[13] 17 CFR 240.19b–4(f)(6).

[14] 17 CFR 240.19b–4(f)(6)(iii).

[15] *Id.*

[16] In approving this rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[17] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42452; File No. SR–NASD–99–41]

Self-Regulatory Organizations; Notice of Filing of Amendment No. 1 to the Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to the Opening of Day-Trading Accounts

February 23, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on February 18, 2000, the National Association of Securities Dealers, Inc. (''NASD''), through its wholly-owned subsidiary, NASD Regulation, Inc. (''NASD Regulation''), filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') Amendment No. 1 to the proposed rule change, File No. SR–NASD–99–41, as described in Items I, II, and III below, which Items have been prepared by NASD Regulation. The NASD submitted the proposed rule change to the Commission on August 20, 1999, which was published in the **Federal Register** on September 21, 1999 (''Original Notice'').[3] The Commission is publishing this notice to solicit comments on Amendment No. 1 to the proposed rule change from interested persons.

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

As described in the Original Notice, NASD Regulation is proposing to amend the 2300 Series of the Rules of the NASD to include new Rule 2360 and Rule 2361 regarding the opening of day-trading accounts. Below is the text of the proposed rule change, as amended. Proposed new language from Amendment No. 1 is in *italics*. Proposed deletions from the language proposed in the Original Notice is in [brackets].

Rule 2360. Approval Procedures for Day-Trading Accounts

(a) No member that is promoting a day-trading strategy, directly or indirectly, shall open an account for or on behalf of a non-institutional customer, unless, prior to opening the account, the member has furnished to the customer the risk disclosure statement set forth in Rule 2361 and has:

[1] 15 U.S.C. 78s(b)(1)

[2] 17 CFR 240.19b–4.

[3] Securities Exchange Act Release No. 41432 (September 14, 1999), 64 FR 51165.

(1) Approved the customer's account for a day-trading strategy in accordance with the procedures set forth in paragraph (b) and prepared a record setting forth the basis on which the member has approved the customer's account; or

(2) Received from the customer a written agreement that the customer does not intend to use the account for the purpose of engaging in a day-trading strategy, except that the member may not rely on such agreement if the member knows that the customer intends to use the account for the purpose of engaging in a day-trading strategy.

(b) In order to approve a customer's account for a day-trading strategy, a member shall have reasonable grounds for believing that the day-trading strategy is appropriate for the customer. In making this determination, the member shall exercise reasonable diligence to ascertain the essential facts relative to the customer, including [his or her financial situation, tax status, prior investment and trading experience, and investment objectives.]:

(1) Investment objectives:

(2) Investment and trading experience and knowledge (e.g., number of years, size, frequency and type of transactions);

(3) Financial situation, including: estimated annual income from all sources, estimated net worth (exclusive of family residence), and estimated liquid net worth (cash, securities, other);

(4) Tax status;

(5) Employment status (name of employer, self-employed or retired);

(6) Marital status; number of dependents; and;

(7) age.

(c) If a member that is promoting a day-trading strategy opens an account for a non-institutional customer in reliance on a written agreement from the customer pursuant to paragraph (a)(2) and, following the opening of the account, knows that the customer is using the account for a day-trading strategy, then the member shall be required to approve the customer's account for a day-trading strategy in accordance with paragraph (a)(1) as soon as practicable, but in no event later than 10 days following the date that such member knows that the customer is using the account for such a strategy.

(d) Any record or written statement prepared or obtained by a member pursuant to this rule shall be preserved in accordance with Rule 3110(a).

(e) For purposes of this rule, the term ''day-trading strategy'' means an overall trading strategy characterized by the regular transmission by a customer of intra-day orders to effect both purchase and sale transactions in the same security or securities.

(f) For purposes of this rule, the term ''non-institutional customer'' means a customer that does not qualify as an ''institutional account'' under Rule 3110(c)(4).

(g) A firm will not be deemed to be ''promoting a day-trading strategy'' for purposes of this Rule solely by its engaging in the following activities:

(1) Promoting efficient execution services or lower execution costs based on multiple trades;

(2) Providing general investment research or advertising the high quality or prompt availability of such general research; and

(3) Having a Web site that provides general financial information or news or that allows the multiple entry of intra-day purchases and sales of the same securities.

Rule 2361. Day-Trading Risk Disclosure Statement

(a) Except as provided in paragraph (b), no member that is promoting a day-trading strategy, directly or indirectly, shall open an account for or on behalf of a non-institutional customer unless, prior to opening the account, the member has furnished to [the] *each* customer, *individually,* in writing or electronically, the following disclosure statement:

You should consider the following points before engaging in a day-trading strategy. For purposes of this notice, a ''day-trading strategy'' means [a] *an overall trading* strategy characterized by the regular transmission by a customer of intra-day orders to effect both purchase and sale transactions in the same security or securities.

- Day trading can be extremely risky. Day trading generally is not appropriate for someone of limited resources and limited investment or trading experience and low risk tolerance. You should be prepared to lose all of the funds that you use for day trading. In particular, you should not fund day-trading activities with retirement savings, student loans, second mortgages, emergency funds, funds set aside for purposes such as education or home ownership, or funds required to meet your living expenses.
- Be cautious of claims of large profits from day trading. You should be wary of advertisements or other statements that emphasize the potential for large profits in day trading. Day trading can also lead to large and immediate financial losses.
- Day trading requires knowledge of securities markets. Day trading requires in-depth knowledge of the securities markets and trading techniques and strategies. In attempting to profit through day trading, you must compete with professional, licensed traders employed by securities firms. You should have appropriate experience before engaging in day trading.
- Day trading requires knowledge of a firm's operations. [You should be familiar with a securities firm's business practices, including the operation of the firm's order execution systems and procedures] Under certain market conditions, you may find it difficult or impossible to liquidate a position quickly at a reasonable price. This can occur, for example, when the market for a stock suddenly drops, or if trading is halted due to recent news events or unusual trading activity. The more volatile a stock is, the greater the likelihood that problems may be encountered in executing a transaction. In addition to normal market risks, you may experience losses due to system failures.
- Day trading may result in your paying large commissions. Day trading may require you to trade your account aggressively, and you may pay commissions on each trade. The total daily commissions that you pay on your trades may add to your losses or significantly reduce your earnings.
- Day trading on margin or short selling may result in losses beyond your initial investment. When you day trade with funds borrowed from a firm or someone else, you can lose more than the funds you originally placed at risk. A decline in the value of the securities that are purchased may require you to provide additional funds to the firm to avoid the forced sale of those securities or other securities in your account. Short selling as part of your day-trading strategy also may lead to extraordinary losses, because you may have to purchase a stock at a very high price in order to cover a short position.

(b) In lieu of providing the disclosure statement specified in paragraph (a), a member that is promoting a day-trading strategy may provide to the customer, *individually*, in writing or electronically, prior to opening the account, an alternative disclosure statement, provided that:

(1) The alternative disclosure statement shall be substantially similar to the disclosure statement specified in paragraph (a); and

(2) The alternative disclosure statement shall be filed with the Association's Advertising Department (Department) for review at least 10 days prior to use (or such shorter period as the Department may allow in particular

circumstances) for approval and, if changes are recommended by the Association, shall be withheld from use until any changes specified by the Association have been made or, if expressly disapproved, until the alternative disclosure statement has been refiled for, and has received, Association approval. The member must provide with each filing the anticipated date of first use.

(c) For purposes of this rule, the term ''day-trading strategy'' shall have the meaning provided in Rule 2360(e).

(d) For purposes of this *R*[r]ule, the term ''non-institutional customer'' means a customer that does not qualify as an ''institutional account'' under Rule 3110(c)(4).

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

In its Original Notice with the Commission, NASD Regulation included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change.[4] The text of these statements may be examined at the places specified in Item IV below. NASD Regulation 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

Background

To address investor protection concerns arising from day-trading activities, NASD Regulation is proposing to amend the NASD rules to include new Rules 2360 and 2361. As described in the Original Notice and Amendment No. 1 herein, the proposed rule change would require a member firm that is promoting a day-trading strategy to furnish a risk disclosure statement to a non-institutional customer prior to opening an account for the customer and either to: (1) Approve the customer's account for a day-trading strategy, or (2) obtain from the customer a written agreement that the customer does not intend to use the account for day-trading purposes. As part of the account approval process, the firm would be required to make a threshold determination that day trading is appropriate for the customer.

In April 1999, NASD Regulation issued *Special Notice to Members* 99–32 (''NTM 99–32'') to solicit comment on the proposed rules regarding approval procedures for day-trading accounts. In response to NTM 99–32, the Association received 39 comment letters. The majority of the letters generally supported NASD Regulation's efforts to address the investor protection concerns raised by individuals engaging in day-trading activities. Commenters, however, raised varied suggestions on how best to regulate day-trading activities and presented disparate views on the scope of the activities that should be covered by the rules. The proposal discussed in NTM 99–32 differed in a number of respects from the proposal subsequently filed with the Commission as the Original Notice.[5]

As indicated in the Original Notice, the Association modified the proposed day-trading rule outlined in NTM 99–32, in response to the comment letters. Many of these changes were significant, and included: limiting the application of the rule to those firms that are ''promoting a day-trading strategy,'' as compared to ''recommending an intra-day-trading strategy''; applying the rule to all non-institutional customers; requiring firms promoting a day-trading strategy to have reasonable grounds for believing that the strategy is appropriate for the customers and to exercise reasonable diligence to ascertain the essential facts relative to the customers; revising the definition of ''intra-day-trading strategy''; requiring firms promoting a day-trading strategy to deliver the risk disclosure statement to all non-institutional customers prior to opening an account for such customers; and revising the risk disclosure statement to include the additional key point that day trading generally is not appropriate for persons of limited resources and limited investment or trading experience and low risk tolerance.

In September 1999, the Commission published the Association's modified proposal, the Original Notice, in the **Federal Register**.[6] The Commission specifically solicited comments on: whether the proposal should cover existing day-trading accounts; whether the proposed definition of ''day-trading strategy'' is appropriate; whether the proposed risk disclosure statement is adequate; and whether the firms should be required to obtain a customer's acknowledgment of receipt of the risk disclosure document.

The Commission received three comment letters in response to the Original Notice. The comment letters were from the Electronic Traders Association (''ETA''), the North American Securities Administrators Association, Inc. (''NASAA''); and the Federal Regulation Committee, the Discount Brokerage Committee and Ad-hoc Committee on Technology & Regulation of the Securities Industry Association (''SIA''). [7] In addition to the specific questions for which the Commission solicited input, the commenters expressed their views on a variety of other issues. Many of the issues raised by the commenters in response to the Original Notice also were raised in the comments in response to NTM 99–32. The comments sent to the Commission are summarized by issue below.

After considering this most recent set of comments, the Association has made additional changes to the subject proposed day-trading rules. The text of the proposed rule language provided herein reflects these changes, which include: modifying the disclosure statement; revising the prescribed method for delivering the disclosure statement; describing certain activities that will not trigger application of the proposed day-trading rules; and clarifying the information-gathering requirements. In addition to describing the proposed amendments, the discussion below clarifies some issues raised by the commenters.

Issues Raised in Comment Letters

Persons Covered by Proposed Rules

As proposed in NTM 99–32, proposed Rules 2360 and 2361 would apply to new customers only. Several

[4] *See supra* note 3.

[5] *Id.*

[6] *Id.*

[7] *See* Letters from James H. Lee, President, Electronic Traders Association (''ETA''), to Jonathan G. Katz, Secretary, SEC, dated October 11, 1999; Bradley W. Skolnik, President, Indiana Securities Commissioner, North American Securities Administrators Association (''NASAA''), to Jonathan G. Katz, Secretary, SEC, dated October 12, 1999; and Lee B. Spencer, Jr., Chairman, Federal Regulation Committee, Everett Lang, Co-Chairman, Discount Brokerage Committee, Michael L. Michael, Chairman, Ad-Hoc Committee on Technology and Regulation, and Michael Anderson, Co-Chairman, Discount Brokerage Committee, Securities Industry Association (''SIA''), to Margaret H. McFarland, Deputy Secretary, SEC, dated October 22, 1999. Each of these commenters represents a group of interested parties. ETA is a trade association of on-site day-trading firms. It has approximately 15 supporting organizations, including six of the ten largest on-site daytrading firms. NASAA is an international organization of securities regulators devoted to investor protection. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. SIA brings together the shared interests of more than 740 securities firms. Its member firms are active in all U.S. and foreign markets and in all phases of corporate and public finance.

commenters to NTM 99–32, including NASAA, responded that all existing customers should be covered by day-trading rules or, at a minimum, receive a risk disclosure statement. On the other hand, several firms argued that the proposal should apply only to new customers because it would be difficult to review all existing accounts to determine which accounts should be classified as day-trading accounts. In its rule filing, the Association revised the proposal so that the day-trading rules would apply to all new accounts. The proposed day-trading rules would not apply to an existing customer, unless the customer opens a new account at a firm that is promoting a day-trading strategy.

In the Original Notice, the Commission solicited comment on whether the proposal should cover existing day-trading accounts. NASAA was the only commenter to respond to this question. NASAA continues to believe that the proposed rules should apply to both new and existing accounts. However, no new arguments were raised in support of this proposition in NASAA's letter. Accordingly, the Association continues to believe that it struck the appropriate balance in the rule filing.

Further, in response to the rule filing, NASAA argues that a requirement to deliver a disclosure statement should apply to all parties whose funds are being handled by third parties. ETA, however, is concerned with how such a requirement would apply to entities such as hedge funds. The Association believes that as a practical matter, it would be difficult (or virtually impossible) for a firm routinely to inquire as to the identity of all parties involved in such arrangements. The Association will continue to examine for abuses involving third parties trading on behalf of others, and notes that such arrangements may raise investment adviser or broker-dealer registration issues.

Definition of Day-Trading Strategy

Proposed Rule 2360, set forth in NTM 99–32, stated that an ''intra-day-trading strategy'' is ''an overall trading strategy characterized by the regular transmission by a customer of multiple intra-day electronic orders to effect both purchase and sale transactions in the same security or securities.'' Several commenters to NTM 99–32 suggested a broader definition, while others suggested limiting the scope of the definition. In its rule filing, NASD Regulation changed the proposed rule language to provide that a ''day-trading strategy'' is ''an overall trading strategy characterized by the regular transmission by a customer of intra-day orders to effect both purchase and sale transactions in the same security or securities.'' The rule filing explained that the Association believes that this definition includes those instances where an individual regularly transmits one or more purchase and sale transactions in a single day. The revised proposal also amended the definition of ''day-trading strategy'' to include orders transmitted by non-electronic means, such as by telephone.

In the Original Notice, the Commission solicited comment on whether NASD Regulation's revised definition of ''day-trading strategy'' is appropriate. NASAA believes that this definition should be further revised to state that a day-trading strategy ''often involves the 'use of margin borrowing and short-selling' and that trading accounts frequently are composed of 'equities' only and contain no long-term time horizon investments.'' The Association, however, believes that the definition included in the rule filing would not benefit from the inclusion of this additional language.

Disclosure Statement

Proposed Rule 2360, set forth in NTM 99–32, stated that the account approval procedures would require the member, prior to effecting an initial day-trading transaction, to provide the disclosure statement contained in proposed Rule 2361 to the customer.[8] The disclosure statement lists several factors that a customer should consider before engaging in day trading, including that the customer should be prepared to lose all of the funds that he or she uses for day trading, and that day trading on margin may result in losses beyond the initial investment. In the rule filing, NASD Regulation revised the proposed disclosure statement to include the additional key point that day trading generally is not appropriate for persons of limited resources and limited investment or trading experience and low risk tolerance.

In the Original Notice, the Commission requested comment on whether the proposed disclosure statement is adequate. NASAA responded by stating that certain structured arrangement entered into by participants of ''day-trading strategies'' may violate laws governing investment advisers. NASAA contends that the disclosure statement should state that persons trading for others may need to register as investment advisers.[9] The purpose of the disclosure statement, however, is to highlight for customers the unique risks posed by their engaging in day trading. The Association believes that the issue of whether an individual trading for others is required to register as an adviser or a broker/dealer should not be addressed in this risk disclosure statement.

ETA supports the concept of a risk disclosure statement. ETA, however, proposes alternative language in three sections of the disclosure statement. First, ETA proposes that the Association replace the following language:

> Day trading requires knowledge of a firm's operations. You should be familiar with a securities firm's business practices, including the operations of the firm's order execution systems and procedures.

ETA proposes the following alternative language:

> Under certain market conditions, you may find it difficult or impossible to liquidate a position quickly at a reasonable price. This can occur, for example, when the market for a stock suddenly drops, or if trading is halted due to recent news events or unusual trading activity. The more volatile a stock is, the greater the likelihood that problems may be encountered in executing a transaction.
>
> In addition to normal market risk, you may experience losses due to system failures. The firm and its clearing broker rely upon sophisticated computer software and hardware to execute transactions, which are subject to failure due to a variety of factors. Among other events, you may experience losses due to: system crashes during both peak and low volume periods; the loss of orders on both SOES and SelectNet; and, delayed, conflicting and inaccurate confirmations on orders or cancellations which you initiate.

In Amendment No. 1, the Association is modifying its proposed disclosure statement based on ETA's comment. NASD Regulation is replacing the language in question with the entire first paragraph and the first sentence of the second paragraph of ETA's recommended language. NASD Regulation believes that this language is an improvement over the language proposed by the NASD.[10] NASD

[8] The firm would be permitted to develop an alternative risk disclosure statement, provided that the alternative statement was substantially similar to the mandated statement and was filed with, and approved by, the Association's Advertising/Investment Companies Regulation Department.

[9] Specifically, NASAA believes that the disclosure statement should ''include a warning that parties who trade the accounts of others, whether through trading authorizations, partnership agreements or otherwise, or who trade with funds furnished by others, whether through pooled fund arrangements or otherwise, and [sic] may be subject to the law and regulations governing investment advisers and may be required to register as investment advisers under state and federal law.''

[10] The NASD is retaining the caption heading for this paragraph: ''Day trading requires knowledge of a firm's operations.''

Regulation, however, believes the remaining language in ETA's recommended second paragraph over emphasizes the fallibility of outside systems.

ETA also proposes alternative language to two other sections of the proposed disclosure statement. ETA recommends changes to the section captioned: ''Day-trading may result in your paying large commissions.'' ETA suggests language which omits any direct reference to total daily commissions possibly adding to an individual's losses. The Association rejects this recommendation because it incorrectly assumes that there will be earnings. Finally, ETA proposes alternative language to the section of the proposed disclosure statement captioned: ''Day-trading can be extremely risky.'' In this section, ETA recommends the Association include a discussion on the difficulty in earning money during the first three to five months of day trading. The Association believes that this language may actually encourage people to continue day trading in hopes that results will improve with time and experience. There does not, however, appear to be any reliable statistical evidence that supports such an assertion.

Finally, in Amendment No. 1, the Association is making a technical revision to the definition of ''day-trading strategy.'' The change is not the product of any of the comment letters. The definition of day trading in the proposed Rule 2361 disclosure statement is being changed to conform with the definition as it appears in the text of proposed Rule 2360.

Customer Acknowledgment

The proposal, set forth in NTM 99–32, would not require customers to sign or otherwise acknowledge receipt of the disclosure statement. Commenters to NTM 99–32 expressed divergent views in response to this issue. Both ETA and NASAA expressed the view that it was appropriate to require a firm to retain a copy of the disclosure document with an acknowledgment of its receipt by the customer. Other commenters argued that the customer should not be required to sign or otherwise acknowledge receipt of the disclosure statement. For instance, E*TRADE argued that the customer's acknowledgment is unnecessary in this context because the statement is a disclosure of risks, and not an agreement between the firm and the customer. After considering the comments, NASD Regulation concluded that it is sufficient for firms to have written procedures in place for delivery of the document and to be able to identify those procedures to any examiners.

In the Original Notice, the Commission solicited comments on whether firms should be required to obtain a customer's acknowledgment of receipt of the disclosure statement. Again, NASAA and ETA expressed the view that customers should be required to acknowledge in writing that they have read and understand the statement. Lastly, NASAA suggests that a principal of the firm sign the statement. In response to these comments, in Amendment No. 1, the Association is revising proposed Rule 2361 to require firms to deliver the disclosure statement to each customer individually, by mail or electronic means, prior to opening the account. This approach would protect against a firm posting the disclosure statement in a remote place on its Web site, and claiming that it was delivered to all customers in such manner. The Association is not proposing to require customers to sign the disclosure statements. The Association believes that any abuses of the delivery requirement could be detected during routine examinations.

Individual Solicitations

As noted above, commenters raised several issues that the Commission did not specifically address in the ''Solicitation of Comments'' section of the rule filing published in the Original Notice. One of these issues is whether the proposed day-trading rule could be triggered only by firms' general promotional efforts, or whether individual solicitations could alone trigger application of the proposed rules. SIA believes that obligations under the proposed rules should not arise in situations where there are no general promotional efforts by firms. SIA argues that ''[i]ndividual solicitations are already covered by suitability and recordkeeping rules and a new rule would not add anything new to investor protection.'' This, however, is not necessarily true if firms are recommending strategies rather than specific securities. Further, SIA argues that ''[e]ven if individually targeted promotions [are] subject to the [proposed day-trading] rule, the rule does not address whether such a promotion would trigger the account opening requirements for *all* new customers of the firm.'' SIA believes that ''in the absence of general promotional efforts, an individual solicitation [should] not trigger obligations under the rule to any customers but those targeted by the promotion.'' It appears that SIA is concerned that the rule filing text could be read to mean that if one broker at a full-service firm targeted, for example, five customers for day trading without the firm's knowledge, then the firm itself would be deemed to be promoting day trading and would need to adhere to the rules for all accounts.

The Association does not believe that such individual solicitations alone would trigger application of proposed Rules 2360 and 2361. Rather, these proposed rules would only be triggered by firms' general promotional efforts or by firm-sponsored promotional efforts. However, firms may not promote day trading through individuals in an effort to circumvent the rules. In addition, if a principal or officer of the firm is aware that brokers in the firm are soliciting customers for day trading, then the firm will be deemed to be promoting day trading.

SIA also notes that the rule filing does not state how long the account review obligation continues after a firm stops promoting a day-trading strategy. Firms, however, working with counsel, if necessary, can reasonably determine whether a sufficient amount of time has passed to remove a firm from coverage of the rules. Finally, SIA seeks ''clarification that the rule[s are] not intended to apply to discretionary or managed accounts, in which brokers execute a variety of strategies that may or may not constitute day trading.'' As noted above, however, the proposed rules would apply only to those firms promoting a day-trading strategy through general or firm-sponsored promotional efforts.

Promoting Day Trading Strategy

As noted above, proposed Rules 2360 and 2361 would apply only to firms ''promoting a day-trading strategy.'' Although the proposed rule language does not define the phrase ''promoting a day-trading strategy,'' the rule filing states that none of the following actions alone would trigger the requirements under the proposed rule change: (1) The promotion by a member of efficient execution services or lower execution costs based on multiple trades; (2) providing general investment research or advertising the high quality or prompt availability of such general research; or (3) having a Web site that provides general financial information or news or that allows the multiple entry of intra-day purchases and sales of the same securities. SIA believes that the day-trading rules should include a safe harbor that codifies the above activity that NASD Regulation does not deem to be ''promoting a day-trading strategy'' for purposes of the rules. SIA recommends including a new paragraph

(g) of Rule 2360 that would state that ''[f]or purposes of this rule, the term 'promoting a day-trading strategy' shall not include [the type of activities listed in the rule filing (and above)].'' [11]

NASD Regulation believes that it would be helpful to describe actions in the text of the proposed rule language that the Association does not consider to be ''promoting a day trading strategy.'' In Amendment No. 1, NASD Regulation is modifying the proposed rule language to state that a member will not be deemed to be ''promoting a day-trading strategy'' for purposes of the rules solely by its engaging in the listed activities.

Other-Use Agreement

As an alternative to approving an account for a day-trading strategy, proposed Rule 2361(a)(2) would permit a firm that is promoting a day-trading strategy to obtain a written agreement from a customer stating that the customer does not intend to use the account for day trading (''other-use agreement'').[12] The firm would be required to provide a risk disclosure statement to the customer even if the firm obtains an other-use agreement. The firm would not be allowed to rely on the other-use agreement if the firm knows the customer intends to use the account for day trading. If the firm opens the account but later knows that the customer is day trading, the firm would then be required to approve the account for day trading.

SIA raises a number of concerns with this provision, including that it ''sets a dangerous precedent by encouraging customers to 'disavow their written pledges with impunity' in order to engage in riskier forms of trading.'' SIA also fears that ''[e]very customer that loses money could claim that he [or she] conveyed an *intention* to day trade, but the firm ignored it.'' They also question how the provision would be interpreted when a firm obtains an other-use agreement from a customer, stops promoting a day-trading strategy, but later knows that the customer is day trading. On balance, the Association believes that the provision is workable and not overly burdensome. The standard is one of actual knowledge, and it seems unlikely that other-use agreements would be widely used at firms that promote day-trading strategies. If a firm stops promoting a day-trading strategy, but later discovers that a customer that provided an other-use agreement is in fact day-trading, the firm should approve that customer for a day-trading strategy. If the firm determines that a day-trading strategy is not appropriate for the person, the firm should prohibit the customer from using the account for day-trading purposes or close the account and return all funds to the customer.

Appropriateness Determination

ETA does not believe that the appropriateness determination for day trading is either useful or necessary. ETA disagrees with the concept that day trading is not appropriate for someone of limited resources and limited investment or trading experience. For example, ETA states that day trading does not require great resources (risk resources of $50,000 to $100,000 are sufficient), and that the proposed rules ignore the benefits provided by training on day-trading techniques. ETA also questions at what point NASD Regulation would consider day traders to be sophisticated given that these traders often make more than 2,000 trading decisions in 30 market days.

The Association does not find ETA's arguments persuasive. The rules are aimed at preventing firms that are actively promoting day-trading strategies from opening accounts for customers who may have limited resources and experience and low risk tolerance. A firm promoting day trading should be required to assess whether a strategy that may require a person to make thousands of trading decisions is appropriate for that individual. The Association recognizes that a person with $50,000 to $100,000 of risk capital may have sufficient resources to open a day-trading account. This factor should be considered as part of the total mix in making the appropriateness determination.

Options Model

ETA argues that the NASD's options rules offer a good model for any proposed day-trading rule. ETA notes that, under the options rules, an individual receives a ''risk disclosure document, signs a new account form verifying the accuracy of the information [the customer has] provided regarding his [or her] finances and market experience, and then, based on this information, is initially allowed to trade the spectrum of available strategies.'' ETA states that ''[t]his sensibly is a one-time analysis, and under the Rule[,] suitability applies only to recommended transactions.'' The day-trading proposal, however, does incorporate many of the same principles contained in the options rules. The appropriateness determination is in fact a one-time analysis to be made by a firm prior to opening the day-trading account.

Further, in Amendment No. 1, the Association is modifying proposed Rule 2360 to incorporate an additional principle from the options rules. The NASD options rules set forth obligations that members must fulfill before conducting certain forms of options trading. NASD Interpretive Material 2860–2 states that in fulfilling their obligations under the NASD rules with respect to options customers who are natural persons, members shall obtain the following information at a minimum: (1) Investment objectives; (2) employment status; (3) estimated annual income from all sources; (4) estimated net worth; (5) estimated liquid net worth; (6) marital status and number of dependents; (7) age; and (8) investment experience and knowledge. The Association is amending proposed Rule 2360 to incorporate a similar information-gathering requirement in the day-trading context.

2. Statutory Basis

NASD Regulation believes that the proposed rule change, as amended, is consistent with Section 15A(b)(6) of the Act [13] in that the proposed rule change is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD Regulation believes that the proposed rule change codifying the obligation of firms promoting day-trading strategies to disclose the risks of these strategies to non-institutional customers and to determine whether the strategy is appropriate for a customer will help to protect investors and the public interest in an increasingly more sophisticated trading environment.

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

NASD Regulation does not believe that the proposed rule change, as amended, 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

The proposed rule change was published for comment in NASD *Special Notice to Members* 99–32 (April 15, 1999). The comment period expired

[11] The actual list of activities in the recommended SIA rule language is a modified version of the language proposed in the Original Notice.

[12] The other-use agreement was proposed in both NTM 99–32 and the rule filing.

[13] 15 U.S.C. 78o–3(b)(6).

on May 31, 1999. Thirty-nine comment letters were received in response to the Notice. Copies of the comment letters and a brief summary of the comment letters have been provided to the Commission. Of the 39 comment letters received, approximately 13 were in favor of the proposed rule change, 8 supported risk disclosure only, 12 were opposed to the proposed rule change, and 6 expressed no opinion or addressed broader issues. Further, on September 21, 1999, the Commission published the Association's modified proposal and solicited comments in the **Federal Register** on the Original Notice. This comment period expired on October 12, 1999. The Commission received three comment letters in response to the Original Notice. Many of the issues raised by the commenters in response to the Original Notice, also were raised in the comments in response to NTM 99–32. After considering this most recent set of comments, the Association is proposing Amendment No. 1 to the rule filing, as outlined above.

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 self-regulatory organization consents, the Commission will:

A. By order approve such proposed rule change, or

B. Institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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 such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to File No. SR–NASD–99–41 and should be submitted by March 23, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[14]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00–4979 Filed 3–1–00; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42461; File No. SR–NASD–99–49]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Regulation ATS

February 25, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on September 21, 1999, the National Association of Securities Dealers, Inc. (''NASD'' or ''Association''), 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 as described in Items I, II, and III below, which Items have been prepared by Nasdaq.[3] 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 proposing to amend Rules 4623 and 4613(e) of the NASD to incorporate the requirements of Regulation ATS into the NASD's rule. Below is the text of the proposed rule change. Proposed new language is in italics; proposed deletions are in brackets.

4623. *Alternative Trading Systems*
[Electronic Communications Networks]

(a) The Association may provide a means to permit *alternative trading systems (''ATSs''), as such term is defined in Regulation ATS, and* electronic communications networks (''ECNs''), as such term is defined in SEC Rule 11Ac1–1(a)(8),

(*1*) to [meet] *comply with SEC Rule 301(b)(3);*

(2) to comply with the terms of the ECN display alternative provided for in SEC Rule 11Ac1–1(c)(5)(ii)(A) and (B) (''ECN display alternatives''); *or*

(3) to provide orders to Nasdaq voluntarily.

In providing any such means, the Association shall establish a mechanism that permits the *ATS or* ECN to display the best prices and sizes of orders entered *into the ATS or ECN* by Nasdaq market makers (and other [entities] *subscribers of the ATS or ECN*, if the ECN *or ATS* so chooses [)] *or is required by SEC Rule 301(b)(3) to display a subscriber's order in Nasdaq*) [into the 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 *ATS or* ECN that seeks to utilize the Nasdaq-provided means to comply with *SEC Rule 301(b)(3)*, the ECN display alternatives, *or to provide orders to Nasdaq voluntarily* shall:

(1) demonstrate to the Association that *it is in compliance with Regulation ATS or* that it qualifies as an ECN meeting the definition in the SEC Rule;

(2) be registered as a NASD member;

(3) enter into and comply with the terms of a Nasdaq Workstation Subscriber Agreement, as amended for *ATSs and* 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 *orders from* other [entities] *subscribers of the ATS or ECN*, if the *ATS or* ECN so chooses [)] *or is required by SEC Rule 301(b)(3) to display a subscriber's order in Nasdaq)*, at the highest buy price and the lowest sell price for each Nasdaq security entered in and widely disseminated by the *ATS or* ECN; and prior to entering such prices and sizes, register with Nasdaq Market Operations as an *ATS or* ECN; [and]

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

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[14] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] On November 10, 1999, Nasdaq filed Amendment No. 1, which refiled the proposed rule change pursuant to Rule 19(b)(2) rather than pursuant to Rule 19(b)(3)(A) and Rule 19b–4(f)(6), as it was originally filed. Letter from Peter R. Geraghty, Assistant General Counsel, the Nasdaq Stock Market Inc., to Richard Strasser, Assistant Director, SEC, Market Regulation, dated November 10, 1999.