

Chapter II, Section 23, "Dealings on Other Exchanges or Publicly Outside the Exchange." Originally, Chapter II, Section 23 prohibited Exchange members from trading over-the-counter in certain securities. Off-board trading restrictions in general provided an additional incentive for members to purchase regional specialist units which promoted internalization of order flow and limited fragmentation.

However, the Commission narrowed the scope of exchange off-board trading restrictions by the adoption of Rules 19c-1 and 19c-3 under the Act.<sup>5</sup> Rule 19c-1 enabled Exchange members to execute agency trades with a market maker who is not an exchange member. Rule 19c-3 permits Exchange members to execute proprietary trades in securities listed after April 26, 1979. On a practical basis, the purchase of a regional specialist unit allowed a member firm to internalize its small retail order flow without violating an exchange's off-board principal trading restrictions.

The Exchange believes it is appropriate to rescind its restrictions on off-board trading at this time. Advances in the application of technology have resulted in the creation of new competitors to the regional exchanges, such as Alternative Trading Systems. As such, the Exchange recognizes the need for exchanges and their members to take part in the greater level of free market trading. The NYSE also filed to rescind NYSE Rule 390. In light of these developments (as well as the Commission's request that the Exchange review its restrictions on off-board trading), the Exchange now proposed to rescind Chapter II, Section 23.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b)(5) of the Act<sup>6</sup> in that it is designed 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 securities, 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; and is not designed to permit unfair discrimination between customers, issuers, brokers, and dealers.

<sup>5</sup> 17 CFR 240.19c-1 and 17 CFR 240.19c-3.

<sup>6</sup> 15 U.S.C. 78f(b)(5).

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

The Exchange believes that the proposed rule change will not 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 approved 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. The Commission also invites interested persons to submit written data, views, and arguments on the market fragmentation issues presented in the NYSE Notice.<sup>7</sup> 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 persons, 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 at the Exchange. All submissions should refer to File No. SR-BSE-00-02 and should be

<sup>7</sup> See supra notes 3 and 4.

submitted by May 8, 2000. Comments responding to the Commission's request for comment on market fragmentation issues should refer to File No. SR-NYSE-99-48 and should be submitted by April 28, 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. 34-42657; File No. SR-CSE-99-05]

### Self-Regulatory Organizations; Order Approving the Proposed Rule Change and Amendment No. 1 to the Proposed Rule Change by the Cincinnati Stock Exchange Enabling Members To Trade Nasdaq/NM Securities

April 10, 2000.

#### I. Introduction

On December 10, 1999, the Cincinnati Stock Exchange ("CSE" or "Exchange") submitted to the Securities and Exchange Commission ("SEC" or "Commission"), 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> a proposed rule change to enable its members to trade Nasdaq/NM securities.

The proposed rule change was published for comment in the **Federal Register** on January 27, 2000.<sup>3</sup> No comments were received on the proposal. On April 7, 2000, the Exchange submitted Amendment No. 1, making several technical changes to the proposed rule text.<sup>4</sup> This order approves the proposed rule change, as amended.

#### II. Description of the Proposal

The proposed rule change would amend the CSE Rules to permit members to trade Nasdaq/NM<sup>5</sup> securities traded on The Nasdaq Stock

<sup>8</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> Securities Exchange Act Release No. 42352 (January 20, 2000), 65 FR 4455.

<sup>4</sup> See letter from Jeffrey T. Brown, Vice President Regulation and General Counsel, CSE, to Heather Traeger, Attorney, Division of Market Regulation, SEC, dated April 4, 2000 ("Amendment No. 1"). Because of the technical nature of this amendment, the Commission is not required to solicit comment on it.

<sup>5</sup> The Exchange amended the text of the proposed rule change to replace "NASDAQ" with "Nasdaq" *id.*

Market ("Nasdaq"), a wholly-owned subsidiary of the National Association of Securities Dealers ("NASD")<sup>6</sup> on an UTP basis.<sup>7</sup> The majority of the proposed rule change to Chapter XI, "Trading Rules," of the CSE rules relates to amendments to accommodate the trading of Nasdaq securities, however, certain changes are housekeeping in nature.

The proposed rule change would amend CSE Rule 11.1, "Hours of Trading" by converting the hours of trading on the Exchange from Cincinnati local time to Chicago local time and providing in subparagraphs (b) and (c) for the inclusion of Nasdaq securities in the determination of trading hours for dually or multiple-traded securities. The changes to CSE Rule 11.2, "Unit of Trading," would reflect the inclusion of Nasdaq securities in determining the appropriate unit of trading. Similarly, the proposed rule change would amend CSE Rule 11.4, "Trading Ex-Dividend, Etc.," and CSE Rule 11.5, "Orders to be Reduced and Increased on Ex-Date," to include Nasdaq securities in the exception language of the rules.

In CSE Rule 11.3, "Price Variations," the proposed rule change would amend the stated minimum variation to reflect the current primary market practice, *i.e.*  $\frac{1}{16}$  of \$1.00 per share in stocks trading at or above \$.50 per share and  $\frac{1}{32}$  of \$1.00 per share in stocks trading below \$.50 per share.<sup>8</sup> The changes would also include securities traded on Nasdaq in determining the appropriate variation. CSE Rule 11.7, "Cabinet Trading," would be amended to reflect that the CSE facilities are now located in Chicago, Illinois.

The proposed rule change would make a number of amendments to CSE Rule 11.9, "National Securities Trading System" ("System"). The amendments to subparagraph (a) would define the terms "Nasdaq/NM Security," "Nasdaq System," "Nasdaq System BBO" and include the term "national securities association" in the definition of "Approved Dealer." The changes to subparagraph (c) would add the term "Nasdaq System BBO" to the definition

of marketable limit order, except Nasdaq/NM securities from the opening guarantee of 1099 shares, and implement a Nasdaq/NM opening guarantee up to 1099 shares at an opening price that is on or between the first unlocked/uncrossed Nasdaq System BBO. The changes to subparagraph (e) would add specialists or market makers who are members of other national securities associations to the entities that may submit bids or offers to the System. The changes to subparagraph (h) would ensure that the System displays the Nasdaq System BBO generated by Nasdaq System market makers<sup>9</sup> and permits Nasdaq System market makers telephonic, or other such access to the System as may be established between the Exchange and the Nasdaq System, and conversely, permit Designated Dealers to send orders from the Exchange via telephone, or by other such access as may be established between the Exchange and the Nasdaq System, to Nasdaq market makers.

Subparagraph (j) of CSE Rule 11.9 would be amended to include the Nasdaq System and the Nasdaq System BBO in the prohibition of executing a limit order only after a regular way transaction occurs in another market at a price equal or inferior to the limit price of the order. The amendments to subparagraph (n) would clarify that the public agency guarantee for 1099 shares at the opening price applies to securities other than Nasdaq/NM securities. However, the public agency guarantee applies to those market and marketable limit orders prices better than the first unlocked/uncrossed Nasdaq System BBO. In addition, the amendments would add the Nasdaq System BBO to the obligations to execute on the basis of the ITS BBO. Finally, the amendments to this subparagraph clarify that the execution guarantees and requirements of CSE Rule 12.6, Customer Priority, apply during the hours of trading on the Exchange (8:30 a.m. to 3:05 p.m. local Chicago time).

The proper rule change would also amend the "Interpretations and Policies" section of CSE Rule 11.9 Interpretation and Policies Section .01. "Market Order Requirement," and .02, "Limit Order Protection Requirement," would be amended to reflect that the obligations of the interpretation apply to securities other than Nasdaq/NM securities.

### III. Discussion

The Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and in particular, with the requirements of Section 6(b).<sup>10</sup> Specifically, the Commission believes the proposal is consistent with the Section 6(b)(5)<sup>11</sup> requirements in that the proposed standards to permit CSE members to trade NASDAQ/NM securities should promote just and equitable principles of trade and facilitate transactions in securities, thereby removing impediments to and perfecting the mechanism of a free and open market in a manner consistent with the protection of investors and the public interest.<sup>12</sup>

Furthermore, the proposed rule change is consistent with Section 12(f)(2) of the Act. Section 12(f)(2) granted the Commission explicit authority to approve UTP in OTC securities. Section 12(f)(2) requires the Commission, prior to approving UTP, to determine that the granting of UTP is consistent with the maintenance of fair and orderly markets and the protection of investors. The Commission believes that the proposed rule change is consistent with these goals and thus, the Commission is approving the proposed rule change, subject to the CSE complying with the requirements of the UTP Plan.

### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>13</sup> that the proposed rule change (SR-CSE-99-05), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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<sup>6</sup> In Amendment No. 1, the Exchange clarified that the proposed rule change permits Exchange members to trade securities traded on Nasdaq, not securities traded on a "national securities association." *Id.*

<sup>7</sup> This filing is made in conjunction with the Exchange joining the Unlisted Trading Privileges Plan ("UTP Plan") governing the collection, consolidation and dissemination of quotation and transaction information for Nasdaq/NM securities. See Securities Exchange Act Release No. 42269 (December 23, 1999), 65 FR 799 (January 6, 2000).

<sup>8</sup> The Exchange represents that these variations will be revisited in any proposed rule changes to accommodate decimal pricing.

<sup>9</sup> In Amendment No. 1, the Exchange clarified that the System does not generate but merely displays the Nasdaq System best bid or offer quotations generated and disseminated by the Nasdaq System. See Amendment No. 1, *supra* note 4.

<sup>10</sup> 15 U.S.C. 78f(b).

<sup>11</sup> 15 U.S.C. 78f(b)(5).

<sup>12</sup> In approving this rule, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>13</sup> 15 U.S.C. 78s(b)(2).

<sup>14</sup> 17 CFR 200.30-3(a)(12).