

information, only the sell-side information will be disseminated, thus avoiding the dissemination of two trade reports for the same trade. The buy-side information that is collected will be used for regulatory purposes.

2. Statutory Basis

The NASD believes that the proposed rule change is consistent with the provisions of section 15A(b)(6) of the Act, which requires among other things, that the NASD's rules must be designed to prevent fraudulent and manipulative acts and practice, to promote just and equitable principles of trade, and in general, to protect investors and the public interest. The NASD's proposed rule change, if approved, will establish additional rules for the reporting of information on eligible fixed income transactions that will provide the NASD, as the self-regulatory organization designated to regulate the over-the-counter markets, with heightened capabilities to regulate the fixed income markets in order to prevent fraudulent and manipulative acts and practices. The proposed rule change, by requiring reporting of such transaction information, will protect investors and the public interest, by among other things, increasing transparency in the fixed income markets.

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

NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended. See the amended statement on burden on competition contained in Amendment No. 4 to SR-NASD-99-65, which also fully applies to this current rule proposal.

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

While comments were neither solicited nor received concerning this rule proposal, several commenters on SR-NASD-99-65 indicated that a dual trade reporting approach for eligible fixed income securities is appropriate.⁵ These comments confirmed that previously proposed rule 6231,

⁵ See Letters from Noland Cheng, Chairman, Fixed Income Transparency Subcommittee of the Securities Industry Association's Operations Committee (December 20, 2000) and Messrs. William H. James, III, 1999 Chairman, Vincent Murray, 2000 Chairman, and Thomas Thees, 2001 Chairman, Corporate Bond Division, The Bond Market Association (December 20, 2000).

contained in the original TRACEE Rules in SR-NASD-99-65, would have required member firms to engage in additional software development efforts and would have required member firms to duplicate the existing clearance data transmission and retention process by re-sending this data to the Association after having sent it to the clearing entities. In light of these comments, the Association is proposing this rule change to require dual trade reporting to the Association for transactions of eligible fixed income securities between two members as a less burdensome approach.

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 Association 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

The Commission invites interested persons 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, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are file 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-01-04 and should be submitted by February 23, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.^b

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 01-2817 Filed 2-1-01; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43893; File No. SR-NASD-01-09]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Implementation of Decimal Pricing in the Nasdaq Market

January 26, 2001.

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 January 25, 2001, 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 ("Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by Nasdaq. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

Nasdaq proposes to modify several NASD rules to support the implementation of decimal pricing in the Nasdaq market as outlined in the Decimals Implementation Plan For the Equities and Options Markets ("Implementation Plan" or "Plan") submitted to the Commission on July 24, 2000. Nasdaq will implement these rule changes pursuant to the Plan starting on March 12, 2001 for each security converted to decimal pricing under the Plan. Securities not trading in decimal increments will continue to be governed by the current fractional versions of these rules. The text of the proposed rule change is below.

Proposed new language is in italics.

* * * * *

^b 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

IM-2110-2. Trading Ahead of Customer Limit Order**(a) General Application.**

To continue to ensure investor protection and enhance market quality, the Association's Board of Governors is issuing an interpretation to the Rules of the Association dealing with member firms' treatment of their customer limit orders in Nasdaq securities. This interpretation, which is applicable from 9:30 a.m. to 6:30 p.m. Eastern Time, will require members acting as market makers to handle their customer limit orders with all due care so that market makers do not "trade ahead" of those limit orders. Thus, members acting as market makers that handle customer limit orders, whether received from their own customers or from another member, are prohibited from trading at prices equal or superior to that of the limit order without executing the limit order. Such orders shall be protected from executions at prices that are superior but not equal to that of the limit order. In the interests of investor protection, the Association is eliminating the so-called disclosure "safe harbor" previously established for members that fully disclosed to their customers the practice of trading ahead of a customer limit order by a market-making firm.

Rule 2110 of the Association's Rules states that:

A member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade.

Rule 2320, the Best Execution Rule, states that:

In any transaction for or with a customer, a member and persons associated with a member shall use reasonable diligence to ascertain the best inter-dealer market for the subject security and buy or sell in such a market so that the resultant price to the customer is as favorable as possible to the customer under prevailing market conditions.

Interpretation

The following interpretation of Rule 2110 has been approved by the Board:

A member firm that accepts and holds an unexecuted limit order from its customer (whether its own customer or a customer of another member) in a Nasdaq security and that continues to trade the subject security for its own market-making account at prices that would satisfy the customer's limit order, without executing that limit order, shall be deemed to have acted in a manner inconsistent with just and equitable principles of trade, in violation of Rule

2110, provided that, until September 1, 1995, customer limit orders in excess of 1,000 shares received from another member firm shall be protected from the market maker's executions at prices that are superior but not equal to that of the limit order, and provided further, that a member firm may negotiate specific terms and conditions applicable to the acceptance of limit orders only with respect to limit orders that are: (a) for customer accounts that meet the definition of an "institutional account" as that term is defined in Rule 3110(c)(4); or (b) 10,000 shares or more, unless such orders are less than \$100,000 in value. Nothing in this interpretation, however, requires members to accept limit orders from any customer.

By rescinding the safe harbor position and adopting this interpretation, the Association wishes to emphasize that members may not trade ahead of their customer limit orders in their market-making capacity even if the member had in the past fully disclosed the practice to its customers prior to accepting limit order. The Association believes that, pursuant to Rule 2110, members accepting and holding unexecuted customer limit orders owe certain duties to their customers and the customers of other member firms that may not be overcome or cured with disclosure of trading practices that include trading ahead of the customer's order. The terms and conditions under which institutional account or appropriately sized customer limit orders are accepted must be made clear to customers at the time the order is accepted by the firm so that trading ahead in the firm's market making capacity does not occur. For purposes of this interpretation, a member that controls or is controlled by another member shall be considered a single entity so that if a customer's limit order is accepted by one affiliate and forwarded to another affiliate for execution, the firms are considered a single entity and the market making unit may not trade ahead of that customer's limit order.

As Outlined in NASD Notice to Members 97-57, the Minimum Amount of Price Improvement Necessary in Order for a Market Maker to Execute an Incoming Order on a Proprietary Basis When Holding an Unexecuted Limit Order for a Nasdaq Security Trading in Fractions, and Not Be Required To Execute the Held Limit Order, Is as Follows:

• *If actual spread is greater than $\frac{1}{16}$ of a point, a firm must price improve an incoming order by at least a $\frac{1}{16}$. For stocks priced under \$10 (which are*

quoted in $\frac{1}{32}$ increments) the firm must price improve by at least $\frac{1}{64}$.

• *If actual spread is the minimum quotation increment, a firm must price improve an incoming order by one-half the minimum quotation increment.*

For Nasdaq securities authorized for trading in decimals pursuant to the Decimals Implementation Plan For the Equities and Options Markets, the minimum amount of price improvement necessary in order for a market maker to execute an incoming order on a proprietary basis in a security trading in decimals when holding an unexecuted limit order in that same security, and not be required to execute the held limit order, is \$0.01.

The Association also wishes to emphasize that all members accepting customer limit orders owe those customers duties of "best execution" regardless of whether the orders are executed through the member's market making capacity or sent to another member for execution. As set out above, the Best Execution Rule requires members to use reasonable diligence to ascertain the best inter-dealer market for the security and buy or sell in such a market so that the price to the customer is as favorable as possible under prevailing market conditions. The Association emphasizes that order entry firms should continue to routinely monitor the handling of their customers' limit order regarding the quality of the execution received.

(b) No Change.

IM-3350. Short Sale Rule.

(a)(1) through (a)(3) No Change.

(b)(1) Rule 3350 requires that no member shall effect a short sale for the account of a customer or for its own account in a Nasdaq National Market security at or below the current best (inside) bid when the current best (inside) bid as displayed by The Nasdaq Stock Market is below the preceding best (inside) bid in the security. The Association has determined that in order to effect a "legal" short sale when the current best bid is lower than the preceding best bid the short sale must be executed at a price of at least $\frac{1}{16}$ th point above the current inside bid when the current inside spread is $\frac{1}{16}$ th point or greater. The last sale report for such a trade would, therefore, be above the inside bid by at least $\frac{1}{16}$ th point. If the current spread is less than $\frac{1}{16}$ th point, however, the short sale must be executed at a price equal to or greater than the current inside offer price.

(2) Moreover, the Association believes that requiring short sales to be a minimum increment of $\frac{1}{16}$ th point above the bid when the current spread is $\frac{1}{16}$ th or greater and equal to or greater

than the offer when the current spread is less than $\frac{1}{16}$ th ensures that transactions are not effected at prices inconsistent with the underlying purpose of the Rule. It would be inconsistent with Rule 3350 for a member or customer to cause the inside spread for an issue to narrow when the current best is lower than the preceding best bid (e.g., lowering its offer to create an inside spread less than $\frac{1}{16}$ th) for the purpose of facilitating the execution of a short sale at a price less than $\frac{1}{16}$ th above the inside bid.

(3) For Nasdaq National Market securities trading in decimals pursuant to the Decimals Implementation Plan for Equity and Options Markets, the Association has determined that in order to effect a "legal" short sale in such securities when the current bid is lower than the preceding bid the short sale must be executed at least \$0.01 above the current inside bid. The last sale report for such a trade would, therefore, be above the inside bid by at least \$0.01.

(c)(1) through (c)(3) No Change.
4632. Transaction Reporting.

(a) through (c) No Change.

(d) Procedures for Reporting Price and Volume.

Members which are required to report pursuant to paragraph (b) above shall transmit last sale reports for all purchases and sales in designated securities in the following manner:

(1) No Change.

(2) No Change.

(3)(A) For principal transactions, except as provided below, report each purchase and sale transaction separately and report the number of shares and the price. For principal transactions which are executed at a price which includes a mark-up, mark-down or service charge, the price reported shall exclude the mark-up, mark-down or service charge. Such reported price shall be reasonably related to the prevailing market, taking into consideration all relevant circumstances including, but not limited to, market conditions with respect to the security, the number of shares involved in the transaction, the published bids and offers with size at the time of the execution (including the reporting firm's own quotation), the cost of execution and the expenses involved in clearing the transaction.

Example:

BUY as principal 100 shares from another member at 40 (no mark-down included);

REPORT 100 shares at 40.

Example:

BUY as principal 100 shares from a customer at $39\frac{3}{8}$ which includes a $\frac{1}{8}$

mark-down from prevailing market at 40;

REPORT 100 shares at 40.

Example:

BUY as principal 100 shares from a customer at 39.90 which includes a \$0.10 mark-down from prevailing market at 40;

REPORT 100 shares at 40.

Example:

SELL as principal 100 shares to a customer at $40\frac{1}{8}$, which includes a $\frac{1}{8}$ mark-up from the prevailing market of 40;

REPORT 100 shares at 40.

Example:

SELL as principal 100 shares to a customer at 40.10, which includes a \$0.10 mark-up from the prevailing market of 40;

REPORT 100 shares at 40.

Example:

BUY as principal 10,000 shares from a customer at $39\frac{3}{4}$, which includes a $\frac{1}{4}$ mark-down or service charge from the prevailing market at 40;

REPORT 10,000 shares at 40.

Example:

BUY as principal 10,000 shares from a customer at 39.75, which includes a \$0.75 mark-down or service charge from the prevailing market of 40;

REPORT 10,000 shares at 40.

(B) No Change.

(e) through (f) No Change.

* * * * *

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

In its filing with the Commission, Nasdaq 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. Nasdaq has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

On June 8, 2000, the Commission ordered the exchanges and the NASD to submit a decimal pricing phase-in plan no later than July 24, 2000. Under the Plan, the NASD is to fully convert the Nasdaq market to decimal pricing no later than April 9, 2001. Before full implementation, Nasdaq is also to commence a decimal pricing pilot program for 10–15 Nasdaq issues on or

before March 12, 2001. Recently, Nasdaq also determined to add a second decimal phase-in of approximately 100+ additional Nasdaq securities on March 26, 2001.

In preparation for decimal pricing, the NASD proposes to amend certain of its rules that contain fractions through the addition of language and decimal-based values so as to govern trading activity in securities that transition from fractional to decimal pricing under the Plan. After Nasdaq's full implementation of decimal pricing, Nasdaq will automatically remove, where appropriate, any remaining fractional references in its rules.³

Specifically, Nasdaq is proposing to amend the following: IM–2110–2 (Trading Ahead of Customer Limit Order); IM–3350 (Short Sale Rule) and NASD Rule 4632 (Transaction Reporting). A summary of the proposed changes is provided below:

IM–2210–2. Trading Ahead of Customer Limit Order

NASD IM–2110–2 ("Manning Interpretation" or "Interpretation") is amended to add language indicating that the minimum amount of price improvement that an NASD member holding an unexecuted limit order in a decimal-priced Nasdaq National Market ("NNM") or SmallCap security must provide when executing an incoming order in that same security to avoid a violation of the Interpretation is \$0.01. The Interpretation is also amended to incorporate the price improvement standard for NMS and SmallCap securities trading in fractions currently contained in NASD Notice to Members 97–57 ("NTM 97–57").

The Manning Interpretation is designed to ensure that customer limit orders are executed in a fair manner and at similar prices at which a firm has indicated it is willing to trade for its own account. To provide customers with the greatest opportunity to have their orders executed, NASD's Manning Interpretation requires NASD member firms to provide a minimum level of price improvement to incoming orders in NMS and SmallCap securities if the firm chooses to trade as principal with those incoming orders at prices superior to customer limit orders they currently hold. If a firm fails to provide the minimum level of price improvement to the incoming order, the firm must

³ Obviously, many NASD Rules and interpretations do not contain, and are not enforced based on, any particular fractional value. Nothing in Nasdaq's move to decimal pricing should be construed as relieving NASD members from their ongoing obligation to comply with all current NASD Rules.

execute its held customer limit orders. Generally, if a firm fails to provide the requisite amount of price improvement and also fails to execute its held customer limit orders, it is in violation of the Manning Interpretation. Currently, the minimum price improvements necessary to avoid a Manning violation, as outlined in NTM 97-57, are:

- If actual spread is greater than $\frac{1}{16}$ of a point = Firm must price improve incoming order by at least a $\frac{1}{16}$. For stocks priced under \$10, (which are quoted in 32nds) the firm must price improve by at least $\frac{1}{64}$.
- If actual spread is the minimum quotation increment = Firm must price improve incoming order by one-half the minimum quotation increment.

In a decimal environment, Nasdaq is proposing the following Manning price improvement standards for NNM and SmallCap securities:

- A firm must always price improve an incoming order by at least \$0.01.⁴

Please note that for securities quoting in decimals, there would no longer be any differentiation between the amount of price improvement required and the price of a particular security.

Nasdaq chose to propose the \$0.01 price improvement standard for securities quoting in decimals, taking the view that the current $\frac{1}{16}$ price improvement values contained in NTM 97-57 discussing the Interpretation generally approximate today's minimum quotation increment for most Nasdaq securities.⁵ One exception to this approach is in the area of Manning price improvement when the spread equals the minimum quote increment. Recognizing that retaining Manning's current " $\frac{1}{2}$ the spread" price improvement alternative standard when the spread equals the minimum quote increment would result in a firm being able to price ahead of a customer order for $\frac{1}{2}$ a penny (\$0.005), Nasdaq has determined to strengthen that standard

and propose a rule that would always require at least a penny price improvement before executing ahead of a held customer limit order. Nasdaq believes that given the size of the new decimal quotation increment, uniform price improvement of a penny, particularly for stocks that are already trading with a penny spread, is an appropriate price improvement standard for the initiation of decimal pricing.

As contemplated in the Plan, Nasdaq and NASD Regulation will closely monitor the protection of customer limit orders during the implementation of decimal pricing in the Nasdaq market and will analyze and evaluate trading activity to determine if future changes to the price improvement standard are warranted.

IM-3350. Short Sale Rule

The Interpretative Material is amended to add language indicating that when the current best bid in a decimalized NNM security is lower than the preceding best bid in that security, a "legal" short sale must be executed at a price at least \$0.01 above the current bid.

NASD's Short Sale Rule requires that no member execute a short sale in an NNM security for a customer or proprietary account at or below the current best bid (unless operating pursuant to an exemption to the rule) when the current best bid is below the preceding best bid in the security. Under the current rule, a valid short sale in an NNM security must be executed at the following specified amounts above the current bid in a down market:

- Spread $\frac{1}{16}$ or greater = Legal Short Sale must be executed at least $\frac{1}{16}$ above current inside bid.
- Spread less than $\frac{1}{16}$ = Legal Short Sale must be executed at price equal or greater than current inside offer.

In a decimal environment, Nasdaq proposes the following standard for "legal" short sales:

- A valid short sale on a down bid would have to be executed at least \$0.01 above the current inside bid.

Nasdaq chose to propose the \$0.01 price improvement standard for legal short sales in decimalized securities in a down market taking the view that the current $\frac{1}{16}$ th values contained in the short sale rule generally approximate today's minimum $\frac{1}{16}$ th quotation increment for most Nasdaq securities.

As contemplated in the Plan, Nasdaq and NASD Regulation will closely monitor the operation of the short sale rule in Nasdaq's decimal environment and will analyze and evaluate trading activity to determine if the short sale price improvement standard adopted

here adequately advances the market quality goals of the rule.

Rule 4632 Transaction Reporting

The Rule is amended to provide alternative reporting examples for securities trading in decimals.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act⁶ in that it is designed to promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to and facilitating transactions in securities, perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

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

Nasdaq does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

Written comments were neither solicited nor received.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

A. by order approve such proposed rule change, or

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

Nasdaq has requested accelerated approval of the proposed rule change. While the Commission will not grant accelerated approval at this time, the Commission will consider granting accelerated approval of the proposal at the close of an abbreviated comment period of 15 days from the date of publication of the proposal in the **Federal Register**.

⁴ Pursuant to the terms of the Implementation Plan, the minimum quotation increment for Nasdaq securities (both National Market and SmallCap) at the outset of decimal pricing is \$0.01. As such, Nasdaq will only display priced quotations to two places beyond the decimal point (to the penny). Quotations submitted to Nasdaq that do not meet this standard will be rejected by Nasdaq systems. See Securities Exchange Act Release No. 43876 (January 23, 2001) (SR-NASD-01-07).

⁵ Originally, Nasdaq's Manning Interpretation required that firm price improve an incoming order by the then minimum trade reporting increment of $\frac{1}{64}$ th. See NASD NTM 94-43 (June 5, 1995). In response to changing market conditions, including a move to a $\frac{1}{16}$ minimum quote increment, Nasdaq adopted the current $\frac{1}{16}$ price improvement standard. See NASD NTM 97-57 (September 1997); Securities Exchange Act Release No. 39049 (September 10, 1997), 62 FR 48912 (September 17, 1997) (SR-NASD-97-66).

⁶ 15 U.S.C. 78o-3(b)(6).

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, 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 Association. All submissions should refer to file number SR-NASD-01-09 and should be submitted by February 20, 2001.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁷

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 01-2850 Filed 2-1-01; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43879; File No. SR-NYSE-00-32]

Self-Regulatory Organizations; Notice of Filing of Amendment No. 1 to a Proposed Rule Change by the New York Stock Exchange, Inc. Relating to Shareholder Approval of Stock Option Plans

January 24, 2001.

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 January 19, 2001, the New York Stock Exchange, Inc. ("Exchange" or "NYSE") filed with the Securities and Exchange Commission ("SEC" or "Commission") an amendment to the proposed rule change³ as described in Items I, II, and

III below, which Items have been prepared by the Exchange. 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

In this amendment, the Exchange proposes two modifications to the Notice. First, the Exchange proposes to extend the effectiveness of the amendments to Sections 312.01, 312.03 and 312.04 of the Exchange's Listed Company Manual with respect to the definition of a "broadly-based" stock option plan, which amendments were approved by the Commission on a pilot basis ("Pilot") on June 4, 1999,⁴ until September 30, 2001.⁵ Second, the Exchange proposes to amend Section 312.04, which defines the term "broadly based." Specifically, the Exchange proposes to amend the requirements regarding awards granted under broadly based plans. The text of the proposed rule change follows. Additions are *italicized*; deletions are [bracketed].

312.00 Shareholder Approval Policy

312.04 For the purpose of Para. 312.03:

* * * * *

(h) A Plan is "broadly-based" if, pursuant to the terms of the Plan:

at least a majority of the company's full-time employees in the United States, who are "exempt employees," as defined under Fair Labor Standards Act of 1938, are eligible to receive stock or options under the Plan; and

at least a majority of the shares of stock or shares of stock underlying options awarded under the Plan[,] during *any three year period* [the shorter of the three-year period commencing on the date the Plan is adopted by the company or the term of the Plan,] must be awarded to employees who are not officers or directors of the company.

Securities Exchange Act Release No. 43111 (August 2, 2000), 65 FR 49046 ("Notice").

⁴ Securities Exchange Act Release No. 41479, 64 FR 31667 (June 11, 1999). The Pilot was originally scheduled to expire on September 30, 2000. On September 22, 2000, the Pilot was extended through November 30, 2000 to accommodate an extended comment period for the Notice. See Securities Exchange Act Release No. 43329, 65 FR 58833 (October 2, 2000). On November 30, 2000, the Pilot was further extended until February 28, 2000. See Securities Exchange Act Release No. 43647 (November 30, 2000), 65 FR 77407 (December 11, 2000).

⁵ The Exchange originally proposed a three-year extension. See Notice, note 3 *supra*.

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

In the Notice, the Exchange requested a three-year extension of the Pilot to permit additional industry discussion of the issues, while at the same time enabling the Exchange to continue to study the experience of NYSE listed companies and their investors under the broadly-based plan rules contained in the Pilot. Following receipt of comments from interested persons and discussion with the SEC staff, the Exchange is amending its proposed to shorten the extension request so that the Pilot will expire on September 30, 2001.

Several commenters on the Pilot also expressed concern that the second part of the broadly definition, which focuses on actual grants made under a plan during either the first three years of a plan or the life of a plan if shorter than three years, does not protect against actions the company may take *after* the first three years. The Commission staff also noted this issue in its order approving the Pilot.⁶

In a letter to the Commission dated March 11, 1999,⁷ the Exchange explained that the three-year formulation was primarily intended to avoid imposing a one-year test. The Exchange further stated that it anticipated that companies would not change their policies after the first three years of a plan. While the Exchange maintains this opinion, it also is willing to remove any lingering concern over this issue by amending the rule to specify that, in order to be "broadly

⁶ See note 4 *supra*.

⁷ See letter from James E. Buck, Senior Vice President and Secretary, NYSE, to Jonathan G. Katz, Secretary, SEC, dated March 11, 1999 (Amendment No. 2 to File No. SR-NYSE-98-32, in which the NYSE proposed the pilot period for the proposed rule change and responded to the comment letters received from interested persons).

⁷ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ The Exchange submitted the proposed rule change on July 13, 2000, which was published in the *Federal Register* on August 10, 2000. See