

NASD members to actively trade in these securities.

The current Program expired on June 30, 2001. Because the Program has helped Nasdaq maintain market share in listed securities, Nasdaq proposes to extend the current Program for an additional six months, through September 1, 2001.

## 2. Statutory Basis

Nasdaq believes the proposed rule change is consistent with Section 15A(b)(6) of the Act,<sup>12</sup> in that the proposal is designed to promote just and equitable principles of trade and to remove impediments to and perfect the mechanism of a national market system, and, in general to protect investors and the public interest. Nasdaq also believes that the proposed rule change is consistent with Section 15A(b)(5) of the Act<sup>13</sup> in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system which the Association operates or controls.

### 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, as amended.

### 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

The proposed rule change has become effective pursuant to Section 19(b)(A)(ii) of the Act<sup>14</sup> and subparagraph (f)(2) of Rule 10b-4 thereunder,<sup>15</sup> because it establishes or changes a due, fee, or other charge imposed by the Association. At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

<sup>12</sup> 15 U.S.C. 78o-3(b)(6).

<sup>13</sup> 15 U.S.C. 78o-3(b)(5).

<sup>14</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>15</sup> 17 CFR 240.196-4(f)(2).

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal 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, 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 the file number SR-NASD-2001-42 and should be submitted by [insert date 21 days from the date of publication].

For the Commission, by the Division of Market Regulations, pursuant to delegated authority.<sup>16</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-44732; File No. SR-NASD-2001-44]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. to Allow ECN and ATS Participation on the OTC Bulletin Board

August 22, 2001.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4<sup>2</sup> thereunder, notice is hereby given that on July 12, 2001, the National Association of Securities Dealers, Inc. ("NASD"), through its 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

<sup>16</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.

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 is proposing to add new NASD Rule 6540(b) to the NASD Rule 6500 Series, which governs the operation of the OTC Bulletin Board ("OTCBB"). The purpose of the proposed rule change is to permit alternative trading systems ("ATSs") and electronic communication systems ("ECNs") to participate in the OTCBB. The text of the proposed rule change is below. Proposed new language is italicized.

\* \* \* \* \*

#### 6540. Requirements Applicable to Market Makers

(a) No change.  
 (b) *An alternative trading system (ATS), as defined in Regulation ATS, Rule 300(a), or electronic communications network (ECN) as defined in SEC Rule 11Ac1-1(a)(8), shall be eligible to participate in the Service, provided however, that such ATS or ECN is an NASD member and otherwise meets the requirements for participation set forth in the OTC Bulletin Board Rules. Where used in the OTC Bulletin Board Rules, the term "market maker" shall be construed to include a participating ATS or ECN.*  
 (c) 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

Nasdaq proposed to permit ATSs and ECNs to post quotes and otherwise participate in the OTCBB. The OTCBB is a quotation service that displays quotes, last-sale prices, and volume

information in over-the-counter ("OTC") securities. OTC securities are equity securities not listed or traded on Nasdaq or a national securities exchange. OTCBB securities include national, regional, and foreign equity issues, warrants, units, American Depositary Receipts, and Direct Participation Programs. Currently, only NASD member firms registered with the NASD as market makers can post quotes for OTC securities on the OTCBB. Nasdaq proposes to broaden participation in the OTCBB by allowing ATSs and ECNs to participate in the OTCBB.

The OTCBB began in 1990 as a pilot program to provide transparency in the OTC equities market.<sup>3</sup> In 1997, the program became permanent.<sup>4</sup> The OTCBB operates pursuant to the NASD Rule 6500 Series. These rules provide, among other things, that all securities quoted on the OTCBB must be sponsored by a participating market maker that registers the security by completing a Form 211, unless an exemption applies. The market maker submits the Form 211 to the NASD OTC Compliance Unit prior to publication of a quote in that security on the OTCBB. Once cleared, Nasdaq Market Data Integrity notifies the market maker that it has been registered in the security and may enter a quote. If the market maker is exempt from Rule 15c2-11 under the Act,<sup>5</sup> the market maker submits a Rule 15c2-11 Exemption Form, which is processed in the same way.

Under proposed Rule 6540(b), an ATS or ECN would be permitted to participate in the OTCBB in the same way that a market maker currently participates. That is, an ATS or ECN that wishes to post a quote in a security on the OTCBB would register the security by completing a Form 211, unless an exemption applies. The ATS or ECN would submit the Form 211 to the NASD OTC Compliance Unit prior to publication of a quote in that security on the OTCBB. Once cleared, Nasdaq Market Data Integrity would notify the ATS or ECN that it has been registered in the security and may enter a quote. If the ATS or ECN is exempt from Rule 15c2-11, the ATS or ECN would submit an alternative form indicating that it is

an ATS or ECN and that it is exempt from Rule 15c2-11.

Every OTC security not currently quoted on the OTC Bulletin Board is considered "ineligible" until a Form 211 or Rule 15c2-11 Exemption Form is submitted. Under the current rules and proposed NASD Rule 6540(b), once clearance to quote the security is given, the security is granted "eligible" status. Thereafter, any other market maker that wishes to quote an "eligible" security must also submit a Form 211 or Exemption Form. An alternative method for obtaining approval to quote an "eligible" security and is exempt from Rule 15c2-11. During the "eligible" period, a frequency-of-quotation test is administered. The test must be satisfied before the security is identified as "active." Once the security is "active," a market maker, ATS, or ECN need not submit a Form 211 or Exemption Form before quoting in the security. To satisfy the test, the security must have been quoted on the OTCBB on at least 12 business days during the preceding 30 calendar days, with not more than four consecutive business days without quotations. Market makers, ATSs, or ECNs would be permitted to register online to quote in a security that has satisfied the test. As long as the security remains "active," any market maker, ATS, or ECN would be permitted to quote the security without a Form 211 or Exemption Form submission.

Nasdaq has stated that one ATS has expressed interest in participating in the OTCBB, and Nasdaq believes that there may be additional ATSs or ECNs interested in participating in the Service. Proposed NASD Rule 6540(b) would permit such participation.

## 2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act.<sup>6</sup> Section 15A(b)(6) requires that the rules of a national securities association, among other things, foster cooperation and coordination with persons engaged in facilitating transactions in securities and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers. Nasdaq believes that the proposed rule, by enabling ATS and ECN participation in the OTCBB, would broaden participation and increase the transparency and liquidity of the OTCBB.

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

Nasdaq does not believe that the proposed rule change would 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 Nasdaq consents, the Commission will:

(A) by order approve such proposed rule change; or

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

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, 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 NASD. All submissions should refer to File No. SR-NASD-2001-44 and should be submitted by September 18, 2001.

<sup>3</sup> See Securities Exchange Act Release No. 27975 (May 1, 1990), 55 FR 19123 (May 8, 1990) (approving SR-NASD-88-19); Securities Exchange Act Release No. 27975A (May 30, 1990), 55 FR 23161 (June 6, 1990) (correcting initial approval order).

<sup>4</sup> See Securities Exchange Act Release No. 38456 (March 31, 1997), 62 FR 16635 (April 7, 1997) (approving SR-NASD-92-7).

<sup>5</sup> 17 CFR 240.15c2-11.

<sup>6</sup> 15 U.S.C. 78o-3(b)(6).

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>7</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-44737; File No. SR-NASD-2001-49]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 by the National Association of Securities Dealers, Inc. To Extend the Expiration Date of Rules Concerning Bond Mutual Fund Volatility Ratings

August 22, 2001.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on August 10, 2001, the National Association of Securities Dealers, Inc. ("NASD" or "Association"), through its wholly owned subsidiary, NASD Regulation, Inc. ("NASD Regulation"), filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I, II and III below, which Items have been prepared by NASD Regulation. On August 16, 2001, NASD Regulation amended the proposal.<sup>3</sup> NASD Regulation filed the proposal pursuant to Section 19(b)(3)(A) of the Act,<sup>4</sup> and Rule 19b-4(f)(6) thereunder,<sup>5</sup> which renders the proposal effective upon with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

<sup>7</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> See August 16, 2001 letter from Patrice M. Gliniecki, Vice President and Deputy General Counsel, NASD Regulation, to Katherine A. England, Assistant Director, Division of Market Regulation, SEC ("Amendment No. 1"). In Amendment No. 1, NASD Regulation (a) clarified that the trial period will be extended through August 31, 2003; (b) clarified that the trial period applies to Rule 2210(c)(3) as well as IM-2210-5; and (c) made technical, non-substantive changes to the proposal.

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>5</sup> 17 CFR 240.19b-4(f)(6). NASD Regulation provided written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, on August 1, 2001.

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

NASD Regulation proposes to amend Interpretive Material ("IM") 2210-5 to extend the expiration date of IM-2210-5 and NASD Rule 2210(c)(3) from August 31, 2001 through August 31, 2003.<sup>6</sup> The text of the proposed rule change is below. Proposed new language is in italics. Proposed deletions are in brackets. IM-2210-5. Requirements for the Use of Bond Mutual Fund Volatility Ratings (This rule and Rule 2210(c)(3) will expire on August 31, [2001] 2003, unless extended or permanently approved by the Association at or before such date.)

(a) No change.

(b) No change.

(c) 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, NASD Regulation included statements concerning the purpose of and basis for its proposal and discussed any comment it received regarding the proposal. 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 and Description of the NASD's Rules on Bond Mutual Fund Volatility Ratings

On February 29, 2000, the SEC approved the adoption of NASD IM-2210-5, which permits members and their associated persons to include bond fund volatility ratings in supplemental sale literature (mutual fund sales material that is accompanied or preceded by a fund prospectus).<sup>7</sup> The SEC also approved at that time, new NASD Rule 2210(c)(3), which sets forth the filing requirements and review procedures applicable to sales literature

<sup>6</sup> In Securities Exchange Act Release No. 42476 (February 29, 2000), 65 FR 12305 (March 8, 2000), the SEC approved IM-2210-5 and NASD Rule 2210(c)(3) on a trial basis. This proposal clarifies in the language of IM-2210-5 that the trial period applies to Rule 2210(c)(3) as well as IM-2210-5.

<sup>7</sup> See Securities Exchange Act Release No. 42476 (February 29, 2000), 65 FR 12305 (March 8, 2000) at 12306.

containing bond mutual fund volatility ratings. Previously, the NASD Regulation staff interpreted NASD rules to prohibit the use of bond fund volatility ratings in sales material.

IM-2210-5 permits the use of bond fund volatility ratings only in supplemental sales literature and only if certain conditions are met:

- The word "risk" may not be used to describe the rating.

- The rating must be the most recent available and be current to the most recent calendar quarter ended prior to use.

- The rating must be based exclusively on objective, quantifiable factors.

- The entity issuing the rating must provide detailed disclosure on its rating methodology to investors through a toll-free telephone number, a web site, or both.

- A disclosure statement containing all of the information required by the rule must accompany the rating. The statement must include such information as the name of the entity issuing the rating, the most current rating and the date it was issued, and a description of the rating in narrative form containing certain specified disclosures.

Rule 2210(c)(3) requires members to file bond mutual fund sales literature that includes or incorporates volatility ratings with the Advertising Regulation Department of NASD Regulation ("Department") at least 10 days prior to use for Department approval. If the Department requests changes to the material, the material must be withheld from publication or circulation until the requested changes have been made or the material has been refiled and approved.

IM-2210-5 and the new Rule 2210(c)(3) were approved on an 18-month trial basis, which trial period expires on August 31, 2001, unless extended or permanently approved by NASD Regulation at or before that date.

#### Proposed Rule Change to Extend the Expiration Date of IM-2210-5 and to Clarify the Related Expiration Date of NASD Rule 2210(c)(3)

As indicated in the SEC's order approving IM-2210-5 and Rule 2210(c)(3), NASD Regulation requested the 18-month trial period to provide an opportunity to assess whether the rule change had facilitated the dissemination of useful, understandable information to investors, and whether it had prevented the dissemination of inappropriate and misleading information.

As of July 2001, the Department had received only six filings pursuant to