

save time and staff resources. In addition, this proposal generally would be less burdensome on the individuals involved, who under the current rules must often appear at two hearings either as the subject or as a witness.

A request to consolidate Minor Rule Violation cases under Rule 17.50(g)(6) could be made to the BCC by any of the persons who were fined or by the Exchange before the start of either of the hearings. In addition, the BCC could decide to consolidate hearings involving the same or a related transaction or occurrence on its own without a request from the parties involved. After receiving a request to consolidate or after deciding to consolidate on its own, the BCC would grant all parties to the hearings a reasonable opportunity to submit a written statement in support of or in opposition to the decision to consolidate a final decision to consolidate would be made by the BCC which would consider all factors deemed relevant, including the staff resources and time that may be saved by the consolidation and whether the consolidation could potentially be prejudicial to the parties involved.

By establishing a procedure to consolidate certain cases involving Minor Rule Violations, the Exchange would be able to save staff resources and time, thereby improving the efficiency with which the Exchange performs its regulatory functions. For these reasons, this policy furthers the objectives of Section 6(b)(7) of the Act in that it is designed to provide a fair procedure for the disciplining of members and persons associated with members. This policy also furthers the objectives of Section 6(b)(5) of the Act in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and to protect investors and the public interest.

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

CBOE does not believe that the proposed rule change will impose any burden on competition.

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

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing of 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. Persons making written submissions should fix copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of the filing will also be available for inspection and copying at the principal office of CBOE. All submissions should refer to the file number of the caption above and should be submitted by August 21, 1996.

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

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 96-19471 Filed 7-30-96; 8:45 am]

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[Release No. 34-37471; File No. SR-NASD-96-17]

Self-Regulatory Organizations; Order Approving Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to the Definitions of Bona Fide Independent Market and Bona Fide Independent Market Maker

July 23, 1996.

I. Introduction

On April 24, 1996, the National Association of Securities dealers, Inc. ("NASD" or "Association") submitted to the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change to Rule 2720 of the NASD's Conduct Rules³ to amend the definitions of "bona fide independent market" and "bona fide independent market maker." A notice of the proposed rule change appeared in the Federal Register on May 24, 1996.⁴ The Commission received one comment letter endorsing the proposed rule change.⁵ The Commission is approving the proposed rule change.

The proposed rule change addresses potential conflicts of interest that arise regarding the conduct of due diligence and the pricing of securities issued by an NASD member, its parent, or an affiliate of a member that is going public ("Rule 2720 offering"). Rule 2720 also would apply to an issuer with which the member has a conflict of interest. The Rule prohibits a member from underwriting or participating in the underwriting or distribution of a Rule 2720 offering of equity or debt unless the price of the equity offering is established no higher, or the yield of the debt offering is established no lower, than the price recommended by a qualified independent underwriter. The qualified independent underwriter also must participate in the preparation of the registration statement and prospectus, offering memorandum, or

¹ 15 U.S.C. § 78s(b)(1) (1988).

² 17 CFR 240.19b-4 (1995).

³ Prior to the NASD *Manual* reorganization, this rule was designated as Schedule E of the NASD's By-Laws. See, NASD *Notice to Members* 96-24 (April 1996).

⁴ Securities Exchange Act Release No. 37223 (May 17, 1996), 61 FR 26239. Also, the NASD granted an extension of the time for Commission action on this rule filing to July 31, 1996. Letter to Katherine A. England, Assistant Director, Division of Market Regulation, SEC, from John Ramsay, Deputy General Counsel, NASD Regulation, Inc. ("NASDR"), dated July 19, 1996.

⁵ Letter from Carter K. McDowell, Assistant General Counsel, BANC ONE Corporation, to Jonathan G. Katz, Secretary, SEC, dated June 13, 1996.

similar document, and exercise the usual standards of "due diligence" regarding the offering. Rule 2720, however, provides an exception from the qualified independent underwriter requirement for offerings of equity securities for which a bona fide independent market exists. Rule 2720 defines a bona fide independent market as a market in a security which has, among other things, at least three bona fide independent market makers.

The NASD reviewed the definitions of bona fide independent market and bona fide independent market maker, which were part of the original version of Rule 2720 when it was adopted as schedule E in 1972. The NASD proposes to revise the definitions to incorporate new requirements for listing, public float, trading volume, price, number of bona fide independent market makers, and limitations on the relationship of the bona fide independent market maker to the issuer that will significantly improve the criteria used for determining if a market of sufficient depth and duration exists to constitute an efficient pricing mechanism for the securities to be distributed. The proposed new definitions will permit members, in appropriate situations, to conduct a secondary offering without the burden and expense of engaging a qualified independent underwriter. However, in situations where the market cannot be relied on to price the securities appropriately, a member would still be required to enlist the services of such an underwriter.

II. Description of the Proposal

Bona Fide Independent Market Definition

Registration Requirement

The proposed rule change retains the current requirement in the definition of bona fide independent market that it must be a market in a security which is registered pursuant to Sections 12(b) or 12(g) of the Act of issued by a company subject to Section 12(d) of the Act.

Price Requirement

The current definition of bona fide independent market does not contain a price requirement. The NASD is concerned that a public float requirement, as set forth below, without a corresponding standard for the market price of the securities does not establish a valid benchmark for a bona fide independent market. Therefore, the NASD is proposing to adopt a new provision in the definition of a bona fide independent market that would require that the security have a market price of at least five dollars (\$5.00) per share as

of the close of trading on the day immediately preceding the filing of the registration statement or offering circular, and have traded at a price of \$5 or more per share on at least 20 of the 30 trading days immediately preceding the date on which the offering circular or registration statement was filed.

Listing and Market Maker Requirements

The current definition of bona fide independent market does not contain a listing requirement. The NASD believes that a listing on a national securities exchange or the Nasdaq Stock Market indicates that the security trades in an efficient, regulated, and active market and strengthens the definition of bona fide independent market by adding the qualitative standards of a regulated trading environment, such as quote transparency and real-time transaction reporting. Therefore, the NASD is proposing to adopt as one of the requirements for the definition of a bona fide independent market that the security, for at least 90 calendar days immediately preceding the filing of the registration statement or offering circular, have been listed on, and is in compliance with, the requirements for continued listing on (i) a national securities exchange, or (ii) The Nasdaq Stock Market so long as such Nasdaq listing has two bona fide independent market makers for a period of at least 30 trading days immediately preceding the filing of the registration statement or offering circular and the effective date of the offering. Securities quoted on the NASD OTC Bulletin Board service and those traded in the general over-the-counter market, such as the "pink sheets," cannot rely on this requirement.

The proposed requirement that the security have at least two bona fide independent market makers for listings on the Nasdaq Stock Market would replace the current requirement of at least three bona fide independent market makers. Given that a security is permitted to be listed on the Nasdaq Stock Market with two market makers, the NASD believes that two market makers are sufficient to demonstrate the presence of a bona fide independent market irrespective of any Rule 2720 affiliate that may also be making a market in the issuer's securities.

Trading Volume and Public Float Requirements

The current definition of bona fide independent market contains independent requirements for trading volume and public float. Under the current rule, a security is considered to have a bona fide independent market if,

for the 12 months immediately preceding the filing of the registration statement, it has *both* an aggregate trading volume of at least 100,000 shares *and* a minimum of 250,000 publicly held shares. Under the proposed rule change, for a bona fide independent market to exist, a security must have for the 90 calendar day period immediately preceding the filing of the registration statement or offering circular *either* an aggregate trading volume of at least 500,000 shares *or* a minimum of 5,000,000 publicly held shares outstanding.

The NASD believes that raising the current aggregate 12-month trading volume requirement from 100,000 shares to 500,000 shares in the 90-calendar-day period before the filing of the registration statement or offering circular provides a criterion that better reflects an active, current and, presumably, efficient market. The increased volume requirement intimates a pricing efficiency which, in turn, establishes a better basis for justifying an exemption from the requirement that a qualified independent underwriter establish the price of the offering.

The NASD considers the alternative requirement of a five-million-share public float as the minimum necessary to ensure that the market for an issuer's securities will not suffer undue volatility from the dilution that occurs when a large number of shares is offered to the public. In this regard, the NASD notes that a typical "follow-on" offering⁶ of a company's stock adds between one- and two-million shares to the public float, which is equal to a 40 percent dilution at the five-million-share level.

Bona Fide Independent Market Maker Definition

The Rule currently defines a bona fide independent market maker as one which meets certain net capital requirements, publishes bona fide bid and ask quotations in a recognized interdealer quotation system, furnishes such quotes to other brokers and dealers on request, and stands ready, willing and able to effect transactions at quoted prices with other brokers and dealers. The current standards of the definition were developed at the time the Rule was adopted in 1972 as Schedule E and were applied to all securities in the over-the-counter market.

The NASD believes that the current standards for the definition of bona fide independent market maker are no longer necessary in light of the proposed

⁶ The term "follow-on" offering refers to a secondary offering of shares by the issuer.

requirement of the definition of bona fide independent market that the security be listed on The Nasdaq Stock Market. Market makers for securities listed on The Nasdaq Stock Market are required to meet certain net capital standards, publish bona fide bid and ask quotations in Nasdaq, which is a recognized interdealer quotation system, furnish quotes to other brokers and dealers on request, and stand ready, willing and able to effect transactions at quoted prices with other brokers and dealers. Therefore, the NASD is incorporating the current requirements into a single standard requiring that the market maker be registered as a Nasdaq market maker.

The NASD believes that the definition of bona fide independent market maker should also provide investors with greater assurance that the market maker's activities are independent of any influences that may arise when the issuer's ownership of securities or interest in the offering become material. Therefore, the NASD is proposing to adopt as part of the revised definition that a bona fide independent market maker (i) must not be a recipient of any of the net proceeds of the offering, (ii) must not be an affiliate of the entity issuing the securities, and (iii) does not in the aggregate itself beneficially own, nor together with its associated persons, at the time of the filing of the registration statement or offering circular, five percent or more of the outstanding voting securities of the entity issuing the securities, if a corporation, or five percent or more of a partnership interest in the distributable profits or losses of the entity, if a partnership.

III. Discussion

The Commission believes that the proposed rule change is consistent with the Act and the rules and regulations promulgated thereunder. Specifically, the Commission believes that approval of the proposed rule change is consistent with Sections 15A(b)(6)⁷ and 15A(b)(9)⁸ of the Act. Pursuant to Section 15A(b)(6), the proposed rule change clarifies and strengthens the criteria for determining a bona fide

independent market and the related concept of a bona fide independent market maker. In so doing, the NASD has removed an impediment to the functioning of a free and open market by improving the criteria used for determining that a market of sufficient depth and liquidity exists to constitute an efficient pricing mechanism for the securities to be distributed. The new definitions also promote economic efficiency because in applicable situations, members will now be able to conduct secondary offerings without incurring the time and expense of engaging a qualified independent underwriter.

The Commission requested clarification from the NASD regarding the term "traded" in proposed paragraph (b)(3)(B) of Rule 2720.⁹ NASDR has confirmed that "traded" encompasses any completed transaction of the day for the security during normal trading hours, up to and including the last reported trade for the day.¹⁰

Pursuant to Section 15A(b)(9), the proposed rule change does not impose any unnecessary or inappropriate burden on competition, but reflects an attempt to update definitions that contain provisions that no longer adequately represent current market practices or pricing. The revised definitions are stringent enough to properly regulate public distributions where a member issues its own securities or where a conflict or control relationship with a parent or affiliate exists, while still providing protection for investors in this type of offering.

IV. Conclusion

For the above reasons, the Commission believes that the proposed rule change is consistent with the provisions of the Act, and in particular with Sections 15A(b)(6) and 15A(b)(9).

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,¹¹ that the proposed rule change (SR-NASD-96-17) be, and hereby is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹²

⁹ The relevant language of paragraph (b)(3)(B) to Rule 2720 is as follows: "... and which has traded at a price of five dollars or more per share in at least 20 of the 30 trading days. . . ."

¹⁰ Letter to Katherine A. England, Assistant Director, Division of Market Regulation, SEC, from Alden S. Adkins, General Counsel, NASD Regulation, Inc., dated July 3, 1996. See also letter to Katherine A. England, Assistant Director, Division of Market Regulation, SEC, from John Ramsay, Deputy General Counsel, NASD Regulation, Inc., dated July 15, 1996, confirming that the definition applies to trades completed during normal trading hours.

¹¹ 15 U.S.C. 78s(b)(2) (1988).

¹² 17 CFR 200.30-3(a)(12).

Margaret H. McFarland,
Deputy Secretary.

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[Release No. 34-37476; File No. SR-NYSE-95-43]

Self-Regulatory Organizations; the New York Stock Exchange, Inc.; Order Granting Approval to Proposed Rule Change Relating to Amendments to Exchange Rules 27, 476(a)(11), and 477

July 24, 1996.

On January 5, 1996, the New York Stock Exchange, Inc. ("NYSE" 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")¹ and Rule 19b-4 thereunder,² a proposed rule change to amend Exchange Rules 27, 476(a)(11), and 477 to require persons under Exchange jurisdiction to comply with information requests from commodities markets and associations and foreign self-regulatory organizations and associations.

The proposed rule change was published for comment in the Federal Register on February 16, 1996.³ No comments were received on the proposal.

Currently, Rule 27 authorizes the Exchange to enter into information sharing agreements with domestic and foreign self-regulatory organizations or associations,⁴ but does not provide for such agreements with commodities regulatory organizations such as contract markets and registered futures associations.

Rule 476(a)(11) permits the Exchange to initiate a disciplinary proceeding against a member, member organization, allied member, approved person, registered or non-registered employee of a member organization or a person otherwise subject to the jurisdiction of the Exchange, for failure to furnish information to, or appear or testify before the Exchange or another domestic self-regulatory organization. The rule

¹ 15 U.S.C. § 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 36831 (Feb. 12, 1996), 61 FR 6279 (Feb. 16, 1996) (notice of File No. SR-NYSE-95-43).

⁴ The Act defines the term "self regulatory organization" as any national securities exchange, registered securities association, or registered clearing agency, or (solely for purposes of sections 19(b), 19(c), and 23(b) of the Act) the Municipal Securities Rulemaking Board established by section 15B of the Act. 15 U.S.C. § 78c(a)(26). Although the Act does not define the term "foreign self-regulatory organization," the NYSE interprets it to include non-U.S. commodities markets. Letter, *infra* note 5.

⁷ Section 15A(b)(6) requires the Commission to determine that a registered national securities association's rules are designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and national market system; and are not designed to permit unfair discrimination among customers, issuers, brokers, or dealers.

⁸ Section 15A(b)(9) requires the Commission to determine that a registered national securities association's rules not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.