

Section 19(b)(2) of the Act. According to the CBOE, the proposed change is consistent with the use of telephones at other locations on the CBOE floor, including at the equity option telephone posts, where the use of telephones is governed by a policy approved by the Commission.²

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, the requirements of Section 6(b)(5)³ in that it is designed to promote just and equitable principles of trade, prevent fraudulent and manipulative acts and practices, and maintain fair and orderly markets.⁴ Specifically, the CBOE has represented that allowing OEX market makers to receive incoming calls from outside the CBOE building may allow OEX market makers to receive information that will assist OEX market makers in performing their duties. In addition, the proposal will make the OEX telephone policy regarding market makers' receipt of incoming calls consistent with the telephone policies at all other trading locations on the CBOE floor.

The Commission believes that it is reasonable for the Exchange to amend its telephone policy for OEX market makers to make the policy consistent with the procedures applicable to all other trading locations on the CBOE has indicated that market makers' receipt of incoming calls at other trading posts on the CBOE floor. In this regard, the Commission notes that the CBOE floor has produced no detrimental effect on the conduct of business at those trading posts. In addition, the CBOE states that the Exchange has not detected any improper trading activity resulting from its telephone policies.⁵ The Commission believes, as it found in approving the CBOE's telephone policy for equity options, that the Exchange's existing surveillance procedures will ensure that the CBOE is aware of any options

transactions that raise manipulation concerns.⁶ Accordingly, the Commission believes that the CBOE's modification of its telephone policy for OEX market makers will not diminish the Exchange's ability to detect and deter manipulation.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. Accelerated approval will allow the CBOE to implement a uniform policy regarding market makers' receipt of incoming calls at their trading posts. Accordingly, the Commission believes that granting accelerated approval to the proposal is appropriate and consistent with Section 6 of the Act.⁷

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and argument concerning the foregoing. 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. 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 from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying at the Commission's Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. Copies of such filing will also be available for inspection and copying at the principal office of the above-mentioned self-regulatory organization. All submissions should refer to File No. SR-CBOE-97-55 and should be submitted by January 7, 1998.

It Is Therefore Ordered, pursuant to Section 19(b)(2) of the Act,⁸ that the proposed rule change (File No. SR-CBOE-97-55) is approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁹

⁶ See Equity Option Approval Order, *supra* note 2.

⁷ 15 U.S.C. 78f.

⁸ 15 U.S.C. 78s(b)(2).

⁹ 17 CFR 200.30-3(a)(12).

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39422; File No. SR-DTC-97-20]

Self-Regulatory Organizations; The Depository Trust Company; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change Expanding the Money Market Instrument Settlement Program

December 19, 1997.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on September 22, 1997, The Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") and on November 13, 1997, amended the proposed rule change (File No. SR-DTC-97-20) as described in Items I and II below, which items have been primarily prepared by DTC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and to grant accelerated approval of the proposed rule change on a permanent basis.

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

The proposed rule change seeks permanent approval of DTC's expanded money market instrument ("MMI") settlement program. The Commission previously approved DTC's expanded MMI program on a temporary basis.

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

In its filing with the Commission, DTC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments that it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. DTC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.²

¹ 15 U.S.C. 78s(b)(1).

² The Commission has modified the text of the summaries prepared by DTC.

² The Commission approved the CBOE's proposal to incorporate its telephone policy for equity options into the rules of the Exchange in 1994. See Securities Exchange Act Release No. 33701 (March 2, 1994), 59 FR 11336 (March 10, 1994) (order approving File No. SR-CBOE-93-24) ("Equity Option Approval Order").

³ 15 U.S.C. 78f(b)(5)(1988).

⁴ In approving this rule, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(b)(5).

⁵ Telephone conversation among Timothy Thompson, Senior Attorney, CBOE, Pat Cerny, Market Surveillance, CBOE, and Yvonne Fraticelli, Attorney, Office of Market Supervision, Division of Market Regulation, Commission, on November 18, 1997 ("November 18 Conversation").

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

DTC's expanded MMI program is an extension of DTC's same-day funds settlement ("SDFS") system. The proposed rule change seeks permanent approval of DTC's expanded MMI settlement program for transactions in institutional certificates of deposit, municipal commercial paper, and bankers' acceptances.³ The proposed rule change also seeks to permanently approve changes made to DTC's MMI programs for corporate commercial paper ("CP"), medium term notes, preferred stock in a CP-like mode, short term bank notes, and discount notes.⁴

The Commission previously granted only temporary approval to the expansion of DTC's MMI settlement program because at the time DTC had not yet implemented the largest provisional net credit ("LPNC") control. The LPNC control consists of two new risk management features which are designed to protect DTC against the combined failure of a MMI issuer and a participant.

Under the first LPNC risk management feature, DTC subtracts from a participant's actual overall SDFS net debit or credit the amount of the participant's largest provisional net credit due to transactions in any single issuer's MMI program. If a transaction causes the resulting net debit ("simulated net debit") to exceed the participant's net debit cap, the transaction will be blocked until the account receives sufficient credits to complete the transaction.

Under the second LPNC risk management feature, DTC subtracts from the participant's collateral monitor the amount of a participant's largest provisional net credit due to transactions in any single issuer's MMI program. If a transaction will cause the resulting collateral monitor ("simulated collateral monitor") to become negative (i.e., the participant's collateral would be insufficient to cover its simulated net debit after the transaction), the transaction will be blocked until the account receives sufficient collateral to complete the transaction.⁵

DTC has reported that MMI issuers have defaulted both before and after the LPNC controls were implemented in September 1995. However, since the implementation of the LPNC controls, DTC stated that it has not had any problems with liquidity or blocked transactions. DTC indicated that the application of LPNC controls may cause some participants to reach their net debit cap and as a result, block the completion of further transactions. However, DTC reported that participants generally complete blocked transactions by sending intraday funds to DTC for credit to their participant settlement account.

DTC believes the proposed rule change is consistent with the requirements of Section 17A of the Act⁶ and the rules and regulations promulgated thereunder because it promotes the prompt and accurate clearance and settlement of transactions in MMIs.

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

DTC does not believe that the proposed rule change will impact or impose a burden on competition.

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

DTC has not solicited comments on the proposed rule change. Discussions with DTC participants indicate continued wide support for the MMI programs.

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

Section 17A(b)(3)(F)⁷ of the Act requires that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible. The Commission believes that DTC's proposed rule change is consistent with DTC's obligations under the Act.

Because the Commission was concerned that the proposed expanded MMI settlement program increased risks associated with the use of provisional credits, the Commission previously approved the proposed rule change on a temporary basis until the new LPNC controls could be implemented and monitored for their effectiveness. During the temporary approval period, the LPNC risk management features have

helped minimize the impact of a default by an MMI issuer. In this regard, since the LPNC controls were implemented in September 1995, DTC has reported that it has had no problems with liquidity or blocked transactions. Thus, the Commission finds that DTC's expanded MMI settlement program, with the addition of the LPNC controls, is consistent with its obligations under the Act to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible.

DTC has requested that the Commission find good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of the filing. The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing because accelerated approval will allow DTC to continue to use its MMI program without interruption.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six 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, 450 Fifth Street, NW., Washington, DC. Copies of such filing will also be available for inspection and copying at the principal office of the above-mentioned self-regulatory organization.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-DTC-97-20) be and hereby is permanently approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁸

³ Securities Exchange Act Release Nos. 33958 (April 22, 1994), 59 FR 22878; and 35655 (April 28, 1995), 60 FR 22423.

⁴ *Id.*

⁵ Because transactions in a failing MMI issue would be reversed by DTC only if DTC is informed of the default by 3:00 PM (Eastern Time), LPNC procedures remain in effect only until approximately 3:05 PM (Eastern Time). After this time, collateralization and net debit cap controls are applied to net debits incurred by participants as a result of transactions that have actually completed.

⁶ 15 U.S.C. 78q-1.

⁷ 15 U.S.C. 78q-1(b)(3)(F).

⁸ 17 CFR 200.30-3(a)(12).

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39423; File No. SR-NASD-97-04]

Self-Regulatory Organizations; Order Approving Proposed Rule Changes and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 2 Thereto Regarding Excused Market Maker Withdrawals and Reinstatements

December 10, 1997.

On January 24, 1997, the National Association of Securities Dealers, Inc. ("NASD" or "Association") filed with the Securities and Exchange Commission ("Commission" or "SEC") proposed rule changes¹ pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange Act")² and Rule 19b-4 thereunder.³ The proposal amends NASD Rule 4619 (excused market maker withdrawals), NASD Rule 4620 (voluntary termination of market maker registrations), and NASD Rule 4730 (reinstatement of market makers that have been "SOESed out of the Box")⁴ or that accidentally withdrew from a security). Notice of the proposed rule changes, including the substance of the proposal and Amendment No. 1 thereto, was published for comment in the **Federal Register**.⁵ No comments were received. On December 3, 1997, the NASD filed with the Commission Amendment No. 2.⁶ The Commission is hereby approving the proposed rule changes,

including Amendment No. 1 thereto. In addition, the Commission is publishing this notice to solicit comments from interested persons on Amendment No. 2; the Commission hereby approves that amendment.

I. Description of Rule Changes

To ensure that market makers are complying with their obligation to maintain continuous, firm, two-sided quotations,⁷ NASD Rule 4620 provides that a market maker that voluntarily terminates its registration in a security may not re-register as a market maker in that security for 20 business days. This rule is commonly referred to as the "20-Day Rule." With respect to SOES, withdrawal from participation as a market maker in a Nasdaq National Market ("NNM") security constitutes termination of registration as a market maker in that security for purposes of NASD Rule 4620. NASD Rule 4730(b)(6), an SOES rule, provides that for NNM securities a market maker will be suspended from SOES if its bid or offer has been decremented to zero due to SOES executions. If this occurs, the market maker will be permitted a standard grace period (*i.e.*, five minutes) within which to take action to restore a two-sided quotation in the security for at least one normal unit of trading. A market maker that fails to reenter a two-sided quotation in an NNM security within the allotted time will be deemed to have withdrawn as a market maker. Unless the market maker's withdrawal is "excused," that market maker may not reenter SOES as a market maker in that security for twenty (20) business days.⁸ When a market maker is deregistered from a security because it failed to restore its quotation, it is referred to as being "SOESed out of the Box."⁹

Notwithstanding NASD Rules 4620 and 4730(b)(6), NASD Rule 4619 permits market makers to obtain an "excused" withdrawal in certain limited circumstances. Under NASD Rule 4619, a market maker may withdraw quotations in a security without being subject to the 20-Day Rule or NASD Rule 4730(b)(6) (for SOES market

makers). A market maker that withdraws from a security for a reason permitted by NASD Rule 4619 may reenter its quotes once the circumstances justifying the withdrawal no longer exist.¹⁰ The rule currently allows excused withdrawals for:

(1) Physical circumstances beyond the market maker's control (NASD Rule 4619(b));

(2) Demonstrated legal or regulatory requirements (*e.g.*, the market maker is in possession of material non-public information regarding the issue) (NASD Rule 4619(b));

(3) Religious holidays (provided the request is submitted five business days in advance of the holiday) (NASD Rule 4619(b));

(4) Vacations (provided the request is received 20 business days in advance of the vacation and is made by a market maker with three or fewer Nasdaq level 3 terminals) (NASD Rule 4619(b));

(5) A market maker that has withdrawn from an issue prior to the public announcement of a merger or acquisition and wishes to re-register in that issue pursuant to applicable NASD rules;

(6) Involuntary failures to maintain clearing arrangements (NASD Rule 4619(c)); and

(7) The duration of the "cooling off" periods mandated by certain rules under Regulation M under the Exchange Act (NASD Rule 4619(d)).

The SEC criticized the NASD's handling of excused withdrawal requests and the reinstatement of market makers that had been "SOESed out of the Box" in the SEC's 21(a) Report on the NASD and The Nasdaq Stock Market.¹¹ The SEC found, among other things, that the NASD had improperly granted waivers of the 20-Day Rule for market makers that were "SOESed out of the Box" and that the NASD had not followed its own rules when granting excused withdrawals. Until 1995, the 21(a) Report found, the practice of Nasdaq Market Operations was to grant SOES withdrawal waivers as a matter of course without inquiring into the reasons for the withdrawals. A market maker merely had to request the waive and Nasdaq Market Operations granted it. Beginning in 1995, Nasdaq Market Operations started to make some inquiry into the reasons for the SOES withdrawals, granting waivers based upon an examination of four factors.¹²

¹ On September 30, 1997, the NASD submitted an amendment ("Amendment No. 1") to the proposed rule change to make technical amendments to the text of the proposed rule change. See Letter from Robert E. Aber, Vice President and General Counsel, The Nasdaq Stock Market, Inc. ("Nasdaq"), to Katherine England, Assistant Director, Division of Market Regulation, Commission, dated September 30, 1997.

² 15 U.S.C. 78s(b)(1).

³ 17 CFR 240.19b-4.

⁴ "SOES" refers to Nasdaq's Small Order Execution System.

⁵ Securities Exchange Act Release No. 39218 (October 8, 1997) 62 FR 53675 (October 15, 1997).

⁶ Letter from Robert E. Aber, Vice President and General Counsel, Nasdaq, to Katherine England, Assistant Director, Division of Market Regulation, Commission, dated December 3, 1997 ("Amendment No. 2"). In Amendment No. 2, the NASD made certain technical changes to NASD Rules 4620 and 4730 as well as clarified certain issues involving NASD Rule 4730. These points are discussed in detail below.

⁷ See NASD Rule 4613.

⁸ NASD Rule 4730(b)(6).

⁹ To avoid being "SOESed out of the Box," members can elect not to have their quote size decremented ("no dec") upon the execution of SOES orders, provided the market maker's quote size is equal to or greater than the applicable SOES tier size (*i.e.*, the maximum SOES order size). See NASD Rule 4730; see also *Nasdaq Subscriber Bulletin*, vol. 15, July 1997, at page 2. In the alternative, the market maker may use Nasdaq's auto-refresh feature, which automatically updates a market maker's quote after its quote size has been decremented. NASD Rule 4730(b)(2).

¹⁰ See NASD Rule 4730(b)(7).

¹¹ See Appendix to Report Pursuant to Section 21(a) of the Securities Exchange Act of 1934 Regarding the NASD and The Nasdaq Stock Market ("21(a) Report"), SEC, August 8, 1996, at p. 91-95.

¹² The factors were (1) the timeliness of the market maker's call to Market Operations; (2) the