

consequences for DTC and its participants. Accordingly, DTC is assessing its own Year 2000 readiness as well as the Year 2000 readiness of all its participants.

Under the proposed rule change, DTC is setting forth a policy statement with respect to DTC's Rule 2. That rule provides the standards and obligations that entities must meet to become DTC participants and to retain their status as participants. Pursuant to Rule 2, a participant must furnish to DTC upon DTC's request information that demonstrates the participant has satisfactory operational capability.

In accordance with Rule 2, DTC will require participants that provide input to DTC through a computer to computer link to conduct a Year 2000 validation test directly with DTC at some point during the first nine months of 1999. Because DTC recognizes the importance in obtaining assurances that participants are individually prepared to receive settlement transaction reports from DTC, input settlement transactions to DTC, and complete settlement, DTC's validation testing process will focus on a limited number of scripted transactions in certain settlement-related areas. The validation test will require participants to process a series of scripted transactions and to balance with DTC's position and settlement statements. DTC will require that each participant provide DTC with a standard testing acknowledgment, signed by a senior internal auditor, that the participant has balanced to the position and settlement statements and has done so in a Year 2000 compliant environment.³

In DTC's view, a participant's failure to successfully complete the Year 2000 validation test will constitute a failure to demonstrate the sufficient operational capability required by Rule 2.

DTC believes that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder because the proposed validation testing will reduce the risk of participant failures caused by computer programs that misinterpret the Year 2000 as the Year 1900. The Year 2000 validation test will help ensure that DTC participants have sufficient operational capability to properly interface with DTC before, on, and after the Year 2000.

³ If a participant does not have an internal auditor, the testing acknowledgment may be executed by a senior compliance officer or other equivalent officer.

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

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

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

The Year 2000 validation test requirement has been received positively by the Securities Industry Association ("SIA") Year 2000 Steering Committee. A draft testing acknowledgment has been reviewed without comment by SIA's Legal and Compliance subcommittee as well as the New York Clearing House Year 2000 Committee.

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

Section 17A(b)(3)(F) of the Act⁴ requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions. The Commission believes that the proposed rule change is consistent with this obligation because the Year 2000 validation test should allow DTC to address any potential problems associated with its participants' Year 2000 readiness. As a result, DTC should be able to continue to provide for the prompt and accurate clearance and settlement of securities transactions before, on, and after Year 2000 without interruption.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the publication of notice of the filing. Approving prior to the thirtieth day after publication of notice should allow DTC and its participants to immediately begin to prepare for DTC's Year 2000 validation testing.

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. 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 20549. Copies of such filing will also be available for inspection and copying at the principal office of DTC. All submissions should refer to the File No. SR-DTC-98-18 and should be submitted by December 21, 1998.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,⁵ that the proposed rule change (File No. SR-DTC-98-18) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁶

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 98-31815 Filed 11-27-98; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40700; File No. SR-DTC-98-16]

Self-Regulatory Organizations; The Depository Trust Company; Order Approving a Proposed Rule Change Modifying the Initial Public Offering Tracking System

November 20, 1998.

On August 19, 1998, The Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change (File No. SR-DTC-98-16) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").¹ notice of the proposal was published in the **Federal Register** on October 21, 1998.² No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description

The rule change modifies DTC's Initial Public Offering ("IPO") tracking system.³ Under the rule change, DTC

⁵ 15 U.S.C. 78s(b)(2).

⁶ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 40552 (October 14, 1998), 63 FR 56279.

³ For a detailed description of the IPO tracking system, refer to Securities Exchange Act Release No.

⁴ 15 U.S.C. 78q-1(b)(3)(F).

will process resales of IPO shares by institutional customers without first determining the identity of the syndicate members that distributed the shares being resold. In addition, DTC will fill stock loans of shares in new issues with shares purchased in the secondary market prior to using shares received in the initial distributions.

I. Resales of IPO Shares by Institutions

DTC's IPO tracking system allows lead managers of new issues to monitor "flipping" of shares in new issues that are distributed through DTC by book-entry movement rather than by use of certificates.⁴ When a lead manager in an IPO notifies DTC of its decision to use the IPO tracking system, the system establishes a database of information about the customers who purchased the IPO shares ("IPO database"). Before DTC processes a resale of IPO shares, the delivering participant must provide to DTC information about its customer. DTC compares the customer information with the customer detail in the IPO database. DTC then reports to the lead manager the identity of the syndicate member whose customer has resold IPO shares.

When IPO shares are sold by a retail customer, the customer information is normally provided by the same participant that populated the IPO database (*i.e.*, the syndicate member). Therefore, the processing of a retail customer's resale of IPO shares is usually not delayed because of a failure to match the identity of the reselling customer with any of the customers included in the IPO database.

In contrast, when IPO shares are distributed to an institutional customer, the syndicate member that makes the distribution is rarely the same participant that acts as the institution's agent for settlement. According to DTC, many redeliveries of IPO shares for institutional customers during the period from three days prior to closing to three days after closing are delayed because the customer detail provided by the institution's agent does not match

any customer in the IPO database.⁵ For example, a failure to match can occur if the syndicate member enters incorrect customer account information (*e.g.*, information with missing digits or transposed characters) into the IPO database because that information will not match the customer account information entered by the reselling institution's agent. A failure to match may also occur when on the day an issue closes an institution's agent attempts to redeliver IPO shares that were not distributed to its participant account until late in the processing day. Ordinarily, the redelivery would be effected if the agent had a sufficient position in an issue. However, if an issue is being tracked by the system, the redelivery will fail because account information relating to the reselling institutional customer will not be resident in the IPO database.

Therefore, under the rule change DTC will process resales of tracked issues by institutional customers without first determining the identity of syndicate members that distributed the shares being resold. DTC has informed the Commission that the IPO tracking system will continue to try to determine the identity of the syndicate members whose institutional customer has resold IPO shares.

2. Stock Loans

Currently, when a participant that has received a distribution of shares in an issue that is being tracked makes a stock loan in that issue, the system attempts to fulfill the stock loan delivery by first using shares received during the initial distribution. DTC then reports these transactions to the lead manager. Under the rule change, DTC will attempt to satisfy the stock loan by first using the lending participant's "secondary market shares" (*i.e.*, shares that have previously been reported to the lead manager as having been "flipped" or shares purchased by the participant in the secondary market). As a result, stock loan transactions will not be reported to the lead manager to the extent that they are processed using secondary market shares.

II. Discussion

Section 17A(b)(3)(F) of the Act⁶ requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and

settlement of securities transactions. The Commission believes that the proposed rule change is consistent with DTC's obligations under Section 17A(b)(3)(F) because it should ensure more efficient processing of trades through the IPO tracking system. Specifically, the rule change should reduce the amount of failed trades in IPO shares that result from processing delays in the IPO tracking system. In addition, the rule change should reduce the amount of processing for loans of IPO shares.

III. Conclusion

On the basis of the foregoing, the Commission finds that DTC's proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-DTC-98-16) be and hereby is approved.

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

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 98-31819 Filed 11-27-98; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40702; File No. SR-MBSCC-98-03]

Self-Regulatory Organizations, MBS Clearing Corporation; Notice of Filing of Proposed Rule Change Relating to an Increase in the Number of Directors

November 23, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on November 5, 1998, MBS Clearing Corporation ("MBSCC") 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 primarily by MBSCC. The Commission is publishing this notice to solicit comments from interested persons on the proposed rule change.

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

The proposed rule change involves an amendment to MBSCC's by-laws to

37208 (May 13, 1996) (order approving proposed rule change).

⁴ Flipping occurs when a syndicate's lead manager is supporting an IPO with a stabilization bid (*i.e.*, the lead manager is purchasing shares in the secondary market in order to keep the price of the issue from dropping below its initial offering price), and shares in the IPO that had been distributed to investors are resold by those investors in the secondary market to a syndicate member. The lead manager may wish to identify flipped transactions so that underwriting concessions (*i.e.*, the discount from the offering price received by syndicate members) can be recovered from the appropriate syndicate members.

⁵ Because shares in new issues can be traded on a when-issued basis, the IPO tracking system allows participants to enter redeliveries of IPO shares as early as three business days prior to the date the issue closes and is distributed through the depository.

⁶ 15 U.S.C. 78q-1(b)(3)(F).

⁷ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).