

market makers.¹² The NASD's current rules capture only those ATSs that meet the definition of ECN. Therefore, the Commission believes that it is necessary to amend these rules to capture those ATSs that do not meet the definition of ECN.

Accordingly, the Commission finds that the proposal is consistent with sections 11A(a)(1)(C) and section 15A(b)(6)¹³ because it will permit Nasdaq to incorporate ATS orders into the Nasdaq quote montage and provide NASD members with the ability to access these orders. In addition, to limit market disruptions caused by locked or crossed markets, the proposal will require members that submit orders to ATSs and ATSs, in certain circumstances, to take reasonable measures before locking or crossing a market. Finally, the amendments will incorporate into the NASD's rules the new obligations imposed on ECNs by Regulation ATS.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,¹⁴ that the proposed rule change (SR-NASD-99-49) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00-14251 Filed 6-6-00; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 42858; File No. SR-NASD-99-05]

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 4 and 5 to the Proposed Rule Change Relating to Margin for Exempted Borrowers, Good Faith Accounts, Joint Back Office Arrangements and Options Transactions

May 30, 2000.

On January 19, 1999, 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 ("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 amending the margin requirements for exempted borrowers, good faith accounts, joint back office ("JBO") arrangements, control and restricted securities, and options transactions. The NASD amended its proposal on June 1, 1999, July 7, 1999, July 15, 1999, October 7, 1999 and April 11, 2000.³ The proposed rule change and Amendment Nos. 1, 2, and 3 were published for comment in the **Federal Register** on August 11, 1999.⁴ The Commission received no comment letters on the proposal. This order approves the proposed rule change, as amended. In addition, the Commission is publishing notice to solicit comments and is simultaneously approving, on an accelerated basis, Amendment Nos. 4 and 5.

I. Description of the Proposal

NASD Regulation proposes to amend NASD rule 2520, "Margin

Requirements," to revise the margin requirements for exempted borrowers, good faith accounts, JBO arrangements, control and restricted securities, and options transactions. NASD Regulation believes that the proposal will conform NASD Rule 2520 to recent changes to NYSE Rule 431 and recently adopted changes to Regulation T.⁵ NASD Regulation is also proposing other minor changes to eliminate obsolete provisions and correct errors in the text of NASD Rule 2520.

A. Margin Requirements for Exempted Borrowers and Good Faith Accounts

Under the recent changes to Regulation T,⁶ the Federal Reserve Board has created a new category of account called the "good faith account" to replace the "non-purpose," "arbitrage," and "government securities" accounts. In the good faith account, a customer may purchase certain securities (exempted and non-equity securities, and money market and exempted securities mutual funds) on "good faith" margin (the amount of margin specified by the creditor in the exercise of sound credit judgment) or the margin specified by the regulatory authority, whichever is greater. Regulation T no longer specifies initial margin, payment and liquidation time frames for transactions in these securities in a good faith account.

NASD Regulation believes that transactions in good faith accounts raise the same safety and soundness questions as transactions in cash and margin accounts. Accordingly, the proposal amends NASD Rule 2520(c) to require all accounts, including good faith accounts, to maintain margin as required by NASD Rule 2520.⁷ Cash accounts will continue to be subject only to certain specific requirements, not to the overall requirements of the rule.

In addition, NASD Regulation states that the Federal Reserve Board established a classification of exempted borrowers which are exempt from Regulation T. An "exempted borrower," as defined in Regulation T, is a broker-dealer "a substantial portion of whose business consists of transactions with persons other than brokers or dealers."⁸ The proposal codifies this exemption

¹² SEC Rule 11Ac1-1(a)(8), 17 CFR 240.11Ac1-1(a)(8).

¹³ 15 U.S.C. 78k-1 and 78o-3(b)(6).

¹⁴ 15 U.S.C. 78s(b)(2).

¹⁵ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Letter from Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), Commission, dated June 1, 1999 ("Amendment No. 1"); Letter from Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, to Katherine A. England, Assistant Director, Division, Commission, dated July 7, 1999 ("Amendment No. 2"); Letter from Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, to Richard C. Strasser, Assistant Director, Division, Commission, dated July 15, 1999 ("Amendment No. 3"); Letter from Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, to Richard C. Strasser, Assistant Director, Division, Commission, dated October 7, 1999 ("Amendment No. 4"); and Letter from Alden S. Adkins, Senior Vice President and General Counsel, NASD Regulation, to Katherine A. England, Assistant Director, Division, Commission, dated April 11, 2000 ("Amendment No. 5"). Amendment No. 1 conforms several provisions of the JBO provisions of NASD Rule 2520, the NASD will interpret the terms "carrying and clearing member" and "carrying member" in the same manner as the NYSE. Amendment No. 1 also provides additional information regarding the proposed changes to the provisions of NASD Rule 2520 governing control and restricted securities. Amendment Nos. 2 and 3 make technical changes to the text of NASD Rule 2520. Amendment No. 4 states that the NASD will allow a six-month phase-in period for implementation of the proposed rule's requirements relating to JBO arrangements. Amendment No. 5 incorporates certain proposed maintenance margin requirements for non-equity securities and options-related requirements that are the subject of related rule filings by NASD Regulation and to ensure consistency with similar proposed changes to NYSE Rule 431.

⁴ See Securities Exchange Act Release No. 41704 (August 4, 1999), 64 FR 43797 (August 11, 1999).

⁵ 12 CFR 220 *et seq.* The Board of Governors of the Federal Reserve System ("Federal Reserve Board") promulgated Regulation T pursuant to Section 7(a) of the Exchange Act, which authorizes it to prescribe regulations relating to credit extensions on securities. See 15 U.S.C. 78g(a).

⁶ See Board of Governors of the Federal Reserve System Docket Nos. R-0905, R-0923, and R-0944, 63 FR 2806 (January 16, 1998).

⁷ See Amendment No. 1, *supra* note 3.

⁸ 12 CFR 220.2.

from Regulation T by excluding "exempted borrowers," as defined in Regulation T, from the definition of "customer" in NASD Rule 2520(a)(3), except for the proprietary account of a broker-dealer carried by a member pursuant to NASD Rule 2520(e)(6). Thus, proprietary accounts of an introducing member that are carried or cleared by another member will remain subject to the equity requirements of NASD Rule 2520(e)(6).

B. Amendments To Provide for Joint Back Office Arrangements

1. Background

Section 220.7(c) of Regulation T⁹ allows special margin treatment for broker-dealers without clearing operations, known as "JBO participants," who invest in a "clearing and servicing" ¹⁰ broker-dealer, known as a "JBO-broker." Under Regulation T, the JBO participants are not treated as "customers" ¹¹ of the JBO broker.

As part of a periodic review of its regulations, in 1995 the Federal Reserve Board proposed an amendment to Regulation T relating to JBO arrangements.¹² The Federal Reserve Board stated that the proposed amendment was prompted by the concerns of several stock exchanges that JBO brokers were extending credit to JBO participants far in excess of their ownership interests in the JBO broker.¹³ Under the proposed amendment, the favorable margin treatment for a JBO arrangement would have been conditioned on the JBO participant's ownership interest in the JBO broker being related to the amount of business transacted through the JBO arrangement.

After Congress enacted the National Securities Market Improvement Act of 1996 ("NSMIA"),¹⁴ the Federal Reserve Board stated that it decided not to adopt its proposed amendment to Regulation T relating to JBO arrangements.¹⁵ Instead, the Federal Reserve Board stated that it "believes it is appropriate to rely on the authority of the JBO's examining authority to ensure the

reasonableness of JBO arrangements under its supervision."¹⁶

2. Original Filing and Amendments Nos. 1-4

NASD Regulation proposes to amend NASD Rule 2520(e)(6) to provide for JBO arrangements established pursuant to section 220.7 of Regulation T. Under the proposal, either a carrying and clearing or carrying broker would be permitted to be a JBO broker.¹⁷ A JBO broker would be required to: (1) Provide written notification to the NASD prior to establishing a JBO arrangement; (2) maintain minimum tentative net capital ¹⁸ of \$25 million as computed under the Net Capital Rule or minimum net capital ¹⁹ of \$7 million if it is engaged in the primary business of clearing options market maker accounts; ²⁰ (3) maintain a written risk analysis methodology for assessing the amount of credit extended to each JBO participant; and (4) deduct from its net capital each JBO participant's haircut requirement under the Net Capital Rule in excess of the equity maintained in the JBO participant's account.

If a JBO broker's tentative net capital or net capital, whichever applies, falls below the prescribed requirement, the JBO broker must (1) promptly notify the

¹⁶ *Id.*

¹⁷ See Letter from Scott Holz, Counsel, Federal Reserve Board, to Raymond J. Hennessey, Vice President, NYSE, dated April 16, 1999 (stating that a carrying firm may be considered a clearing and servicing firm within the meaning of the JBO provisions of Regulation T).

¹⁸ The term "tentative net capital" generally refers to net capital before haircuts and undue concentration charges on proprietary securities and options positions. Haircuts are specified percentages of the market value of a broker-dealer's proprietary securities by which a broker-dealer must reduce its net worth under Exchange Act Rule 15c3-1 (the "Net Capital Rule").

¹⁹ The term "net capital" is defined under the Net Capital Rule and is generally calculated by deducting illiquid assets from a firm's "net worth," as determined under Generally Accepted Accounting Principles (GAAP), adding to that amount properly subordinated debt under Appendix D of the Net Capital Rule, and further deducting haircuts from securities held in the firm's proprietary accounts.

²⁰ Under the proposal, the clearance of options market maker accounts would be deemed a broker-dealer's primary business if a minimum of 60% of the aggregate deductions in its ratio of gross options market maker deductions to net capital (including gross deductions for JBO participant accounts) are options market maker deductions. Subparagraph (c)(2)(x) of the Net Capital Rule limits the amount of specialist and market maker options positions a firm may guarantee, endorse or carry to a ratio of 10 to one of options market maker and specialist deductions to net capital. In addition, subparagraph (a)(6) of the Net Capital Rule exempts an option market maker and specialist from the haircut provisions of the Net Capital Rule provided that, among other things, the firm maintains an account liquidating equity equal to the percentage described in subparagraph (a)(6)(iii)(A) of the Net Capital Rule.

NASD in writing of the deficiency; and (2) resolve the net capital deficiency within three business days. If a JBO broker fails to correct a net capital deficiency within three business days it would not be permitted to accept new transactions through the JBO arrangement.

A JBO participant must be a registered broker-dealer subject to the Net Capital Rule and must maintain an ownership interest in its JBO broker in accordance with Regulation T. The JBO participant must maintain in the JBO arrangement a minimum of \$1 million in liquidating equity, exclusive of the JBO participant's ownership interest in the JBO broker required under Regulation T. If a JBO participant's liquidating equity falls below \$1 million, it must cure the deficiency within five business days or lose its JBO participant status. Unless the JBO participant was an "exempted borrower," ²¹ a JBO participant that lost its JBO participant status would become subject to the margin requirements prescribed for customers in Regulation T and other maintenance margin requirements under NASD Rule 2520.²²

NASD Regulation will allow a six-month phase-in period for implementation of the requirements relating to JBO arrangements. NASD Regulation believes that the six-month phase-in will allow sufficient time for members and member organizations to comply with the new capital and risk analysis requirements and to implement new or make changes to existing arrangements or systems.²³

3. Amendment No. 5

Amendment No. 5 proposed to incorporate a related rule change (the "Exempt Account Proposal") into the current proposal.²⁴ Under the Exempt Account Proposal, a broker-dealer's maintenance margin requirement would be reduced below the haircut requirement under the Net Capital Rule for certain non-equity securities held in

²¹ The term "exempted borrower" is defined in section 220.2 of Regulation T. NASD Rule 2520(a)(3), as revised by the current proposal, specifically excludes an exempted borrower from its definition of customer.

²² See Amendment No. 5, *supra* note 3.

²³ See Amendment No. 4, *supra* note 3.

²⁴ In the Exempt Account Proposal (File No. SR-NASD-00-08), the NASD proposes to amend NASD Rule 2520(e)(2)(F) and to adopt NASD Rule 2520(e)(2)(G) to revise the margin requirements for certain non-equity securities held in "exempt accounts," as defined in the proposal. The NASD filed the Exempt Account Proposal with the Commission on March 3, 2000. To date, the Commission has not taken action on the Exempt Account Proposal. Accordingly, this order does not approve the Exempt Account Proposal or its application to the margin requirements contained in this filing.

⁹ 12 CFR 220.7(c).

¹⁰ Regulation T does not define the term "clearing and servicing." However, Regulation T describes a JBO broker as a clearing and servicing firm.

¹¹ The term "customer" is defined in section 220.2 of Regulation T.

¹² Board of Governors of the Federal Reserve System Docket No. R-0772 (June 21, 1995), 60 FR 33763 (June 29, 1995).

¹³ *Id.*

¹⁴ National Securities Markets Improvement Act of 1996, Pub. L. 104-209, 110 Stat. 3416 (October 11, 1996).

¹⁵ Board of Governors of the Federal Reserve System Docket No. R-0772 (April 24, 1996), 61 FR 20386 (May 6, 1996).

an exempt account. Under Amendment No. 5 to the current proposal, a JBO broker would be permitted to alternatively deduct from its net capital the difference between a JBO participant's account equity and the maintenance margin requirement under the Exempt Account Proposal, as opposed to the haircut requirement under the Net Capital Rule originally proposed. The NASD stated that this amendment would establish consistency by incorporating the most recent maintenance margin requirements of the Exempt Account Proposal into the JBO filing.²⁵

C. Reduced Margin for Specialist, Market Maker, and Broker-Dealer Accounts

NASD Rules 2520(e)(5) and (e)(6) currently require a carrying broker-dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker or broker-dealer and the required maintenance margin under NASD Rule 2520. The NASD proposes to amend subparagraphs (e)(5) and (e)(6) to require the carrying broker-dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker or broker-dealer and the required haircut in accordance with the Net Capital Rule.²⁶

D. Control and Restricted Securities

The "Concentration Reduction" provision in NASD Rule 2520(e)(8)(C)(ii) is designed to impose increasing margin requirements for customer positions in control and restricted securities based upon the percent of outstanding shares or the percent of average weekly volume that the position represented. However, the NASD believes that the provision unintentionally penalizes a customer for maintaining a position that exceeds the collateral necessary to cover his margin loan. To eliminate this unintended penalty, the proposed rule excludes "excess securities" from the concentration reduction calculation. The proposal defines "excess securities" as the amount of securities, if any, by which the aggregate position in control and restricted securities of any one issue

exceeds the aggregate amount of securities that would be required to support the aggregate credit extended on such control and restricted securities if the applicable margin requirement were 50%. Thus, under the proposed rule change, the concentration reduction calculation will be performed on an aggregate position that is only as large as the collateral necessary to support a margin loan of 50%.

In addition, the proposed rule change expands the exception in paragraph (e)(8) to include all restricted securities that are then saleable, including affiliate securities, pursuant to SEC Rules 144(k), 145(d)(2), or 145(d)(3). Accordingly, those customer-owned, restricted securities that are then saleable can be sold under SEC Rule 144(k) would be subject to the same maintenance margin requirements that presently apply to ordinary stock (25%).

E. Amendments to Margin Rules Governing Options Transactions

NASD Regulation is proposing to amend NASD Rule 2520(f)(2) to add subparagraphs (L) and (M)(i), which are identical to current provisions in NYSE Rule 431(f)(2)(L) and (f)(2)(M)(i).²⁷ Proposed NASD Rule 2520(f)(2)(L) will allow a customer to designate which security position in an account will be utilized to cover the requested margin at the time the option order is entered, provided the member offers such a service. Proposed NASD Rule 2520(f)(2)(M)(i) will permit options transactions in customer cash accounts if the transaction is permissible under section 220.8 of Regulation T.

II. Discussion

For the reasons discussed below, the Commission finds that the proposed rule change, as amended, is consistent with the Exchange Act and the rules and regulations under the Exchange Act applicable to a national securities association. In particular, the Commission believes that the proposed rule change is consistent with section 15A(b)(6) of the Exchange Act,²⁸ which requires the rules of an association be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and to protect investors and the public interest.²⁹

A. Exempted Borrowers and Good Faith Accounts

The Commission finds that it is reasonable for the NASD to amend NASD Rule 2520(c) to apply the existing maintenance margin requirements of NASD Rule 2520 to transactions in "good faith" accounts permitted under Regulation T. Although transactions permitted in a good faith account will not be subject to the initial margin requirements, payment requirements and liquidation time frames of Regulation T, as the NASD notes, transaction in a good faith account may raise the same safety and soundness concerns with regard to maintenance margin as do transactions in margin accounts. Accordingly, the Commission believes that applying the maintenance margin requirements of NASD Rule 2520(c) to transactions in a good faith account will protect investors and the public interest and help to maintain fair and orderly markets by ensuring that good faith accounts contain adequate margin reserves. The Commission notes that it approved a similar change to NYSE Rule 431(c).³⁰

In addition, the Commission believes it is reasonable for the NASD to amend the definition of "customer" in NASD Rule 2520(a)(3) to codify the NASD's position that exempted borrowers, as defined under Regulation T, will remain exempt from the requirements of NASD Rule 2520, except for the proprietary accounts of a broker-dealer carried by a member pursuant to NASD Rule 2520(e)(6). The Commission believes that it is reasonable for the NASD to continue to apply the equity requirements of NASD Rule 2520(e)(6) to the proprietary accounts of broker-dealers that qualify as "exempted borrowers" under Regulation T and that are carried by another NASD member. By continuing to apply the equity requirements of NASD Rule 2520(e)(6) to these proprietary accounts, the Commission believes that the proposal will help to ensure that these accounts contain adequate margin, thereby protecting investors and the public interest. The Commission notes that it approved an identical change to the definition of "customer" in NYSE Rule 431(a)(2).³¹

B. JBO Provisions

The Commission believes that NASD Regulation has proposed reasonable

on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

³⁰ See Securities Exchange Act Release No. 40529 (October 7, 1998), 63 FR 55567 (October 16, 1998) ("1998 Order").

³¹ See 1998 Order, *supra* note 29.

²⁵ See Amendment No. 5, *supra* note 3.

²⁶ For example, in the case of a long position in an equity security, the proposal would require a carrying broker to compute its net capital deduction for deficient specialist, market maker and broker-dealer accounts based on the 15% haircut requirement of paragraph (c)(2)(vi)(j) of the Net Capital Rule, rather than the 25% maintenance margin requirement of NASD Rule 2520(c)(1).

²⁷ In Amendment No. 5, NASD Regulation revised its proposal to delete proposed subparagraph (f)(2)(M)(ii). On March 31, 2000, NASD Regulation filed a revised version of proposed subparagraph (f)(2)(M)(ii) in File No. SR-NASD-00-15. The Commission has not taken action on that proposal.

²⁸ 15 U.S.C. 78o-3(b)(6).

²⁹ In approving the proposed rule changes, the Commission has considered the proposal's impact

capital and equity requirements for JBO brokers and JBO participants. The Commission also believes that the proposed rule change fulfills the Federal Reserve Board's mandate for the SROs to provide rules that "ensure the reasonableness of JBO arrangements."³²

With respect to JBO brokers, the Commission believes that it is reasonable for the Association to require a JBO broker to: (1) Provide written notification to the Association prior to establishing a JBO arrangement; (2) provide prompt written notification to the Association if its tentative net capital or net capital, whichever applies, falls below the prescribed requirements; (3) resolve any net capital deficiency within three business days or not be permitted to accept additional transactions through the JBO arrangement; (4) maintain a written risk analysis methodology for assessing the amount of credit extended to each JBO participant; and (5) deduct from its net capital each JBO participant's haircut requirement in excess of the equity maintained in the JBO participant's account.³³ In addition, the Commission believes that it is reasonable for the Association to require a JBO broker to maintain a minimum of \$25 million in tentative net capital or \$7 million in net capital if the JBO broker's primary business is clearing options market maker accounts. The Commission also believes that it is reasonable to deem a broker-dealer's primary business to be the clearance of options market maker accounts if a minimum of 60% of its aggregate deductions in its ratio of gross options market maker deductions to net capital (including gross deductions for JBO participant accounts) are options market maker deductions.

In addition, the Commission believes that it is reasonable for the NASD to require a JBO broker to immediately notify the NASD if its tentative net capital or net capital, whichever applies, falls below the prescribe minimum levels. The Commission also believes that it is reasonable for a JBO broker to be subject to the equity capital withdrawal restrictions of paragraph (e) of the Net Capital Rule and the prohibitions against the reduction, prepayment, and repayment of subordination debt of paragraph (b) of Appendix D of the Net Capital Rule, as if the firm's net capital would be below

the minimum standards specified by those sections.

The Commission believes that the \$7 million net capital requirement for JBO brokers is a reasonable response to the need for a capital cushion for the fluctuations in net capital resulting from the daily changes in JBO participant accounts and would avoid unnecessary and inadvertent violations of the net capital requirements at the times when a firm's capital needs are more volatile, such as the week that options expire or during severe market stresses.

The Commission believes that it is reasonable for the Association to require a JBO broker to be either a clearing and carrying, clearing, or carrying firm in accordance with the requirements under Regulation T and the Federal Reserve Board's applicable interpretations.

With respect to JBO participants, the Commission believes that it is reasonable for the Association to require a JBO participant to: (1) Be a registered broker-dealer subject to the Net Capital Rule; (2) maintain an ownership interest in the JBO Broker in accordance with Regulation T; and (3) maintain a minimum liquidating equity of \$1 million in the JBO arrangement. The Commission also believes that it is reasonable to require a JBO participant whose liquidating equity falls below the required \$1 million to deposit the deficiency within five business days or lose its JBO participant status and become subject to the customer margin account requirements under Regulation T and the other NASD maintenance margin requirements.

The Commission believes that the requirement of \$1 million equity in the account is not unreasonable, considering the lack of regular maintenance margin requirements and the substantial leverage that would be obtained by the JBO participant.

The Commission believes that it is important for the Association to be adequately prepared to implement and monitor the revised rules. Therefore, the Commission believes that it is appropriate to permit firms to allow a six-month phase-in of these new rules relating to JBO arrangements.

C. Reduced Margin for Specialist, Market Maker and Broker-Dealer Accounts

The Commission believes that it is reasonable to require a broker-dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker and broker-dealer and the required haircut in

accordance with the Net Capital Rule.³⁴ The Commission believes that it is appropriate and equitable for SROs to require the same maintenance margin requirements for specialist, market maker and broker-dealer accounts as JBO participant accounts.

D. Concentration Provisions for Control and Restricted Securities

The Commission believes that it is reasonable for the NASD to permit a firm to deduct the amount of its customers' excess control and restricted securities in determining if a concentration of control and restricted securities exists for purposes of deducting from its net capital any margin deficiencies in a customer's account under subparagraph (e)(8)(B)(i) of NASD Rule 2520. Excess securities includes securities by which a customer's aggregate position in control and restricted securities of any one issue exceeds the aggregate amount of securities that would be required to support the aggregate credit extended on those securities, assuming a 50% margin requirement.

The Commission notes that the current concentration provisions for control and restricted securities appear to be inappropriate because they impose stricter requirements on accounts that have more control and restricted securities than necessary to collateralize a credit extension. By limiting the determination of whether a concentration of control and restricted securities exists to two times the credit extension, the proposal would subject these securities to a greater margin requirement based only on financed control and restricted securities. The Commission believes that this is a reasonable and appropriate margin requirement.

The Commission also believes that it is reasonable for the NASD to exempt affiliate securities from the margin provisions relating to control and restricted securities provided that the securities otherwise meet the requirements of subparagraph (e)(8)(D), including that: (1) The securities are considered then saleable under Securities Act Rule 144(k), Securities Act Rule 145(d)(2) or Securities Act Rule 145(d)(3); and (2) the issuer is current in its filings pursuant to the continuous disclosure system under the Act.

The Commission notes that its interpretations under Securities Act

³² See Board of Governors of the Federal Reserve System Docket No. R-0772 (April 24, 1996), 61 FR 20386 (May 6, 1996).

³³ To date, the Commission has not taken action on the NASD's Exempt Account Proposal. Accordingly, this order does not approve the Exempt Account Proposal or its application to the margin amendments contained in this filing.

³⁴ As noted above, this order does not approve NASD's Exempt Account Proposal on its application to the margin requirements contained in this filing.

Rule 144(k) may, under certain circumstances, permit a broker-dealer to sell control and restricted securities of an affiliate in default without regard to the volume and other restrictions imposed on affiliates. In addition, subparagraph (d)(3)(iv) of Securities Act Rule 144 permits a broker-dealer to "tack" the ownership period of an affiliate in default to its own for purposes of determining if the time conditions of Securities Act Rule 144(k) are met. Accordingly, the Commission believes that it is appropriate for affiliate securities, which otherwise meet the requirements subparagraph (e)(8)(D), to be exempt from the maintenance margin rules for control and restricted securities.

E. Amendments to Margin Rules Governing Options Transactions

The NASD proposes to amend Rule 2520(f)(2) to add subsections (L) and (M)(i). Section 2520(f)(2)(L) incorporates the provisions currently contained in Regulation T regarding "exclusive designation" that allow a customer to designate which security position in an account is to be utilized to cover the required margin at the time an option order is entered, provided the member organization offers such a service. This section merely incorporates existing provisions of Regulation T into the NASD rule and, accordingly, is reasonable. The Commission notes that it approved an identical change to NYSE Rule 431.³⁵

Further, proposed NASD Rule 2520(f)(2)(M)(i) does not raise new regulatory issues because it incorporates those provisions of Regulation T that allow certain defined options-related transactions to be maintained in a cash account. The Commission notes that it approved a similar change to NYSE Rule 431.³⁶

F. Accelerated Approval of Amendment Nos. 4 and 5

The Commission finds good cause for approving Amendment Nos. 4 and 5 prior to the thirtieth day after the date of publication of notice of filing therefore in the **Federal Register**. Amendment No. 4 proposes a six-month phase-in of the rule changes relating to JBO arrangements. The Commission believes that this amendment is necessary because it is important for the NASD and its members to be adequately prepared to implement and monitor the

new rules relating to JBO arrangements. Amendment No. 5 clarifies the proposal by incorporating references to the Exempt Account Proposal, and deleting a proposed change to NASD Rule 2520(f)(2)(m)(ii), which has been superseded by a change to subparagraph (f)(2)(m)(ii) proposed in File No. SR-NASD-00-15. Accordingly, the Commission finds it is consistent with sections 6(b)(5) and 19(b) of the Exchange Act to approve Amendment Nos. 4 and 5 on an accelerated basis.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning Amendment Nos. 4 and 5, including whether Amendment Nos. 4 and 5 are 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 submissions, 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 persons, 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 the NASD. All submissions should appropriately refer to SR-NASD-99-05.

IV. Conclusion

It Is Therefore Ordered, pursuant to Section 19(b)(2) of the Exchange Act,³⁷ that the proposed rule change, SR-NASD-99-05, as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.³⁸

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00-14252 Filed 6-6-00; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-42876; File No. SR-NASD-99-69]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. Clarifying Certain Listing Standards of the Nasdaq Stock Market, Inc.

May 31, 2000.

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 November 22, 1999, 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 ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. The Association submitted Amendments No. 1³ and No. 2⁴ to the proposed rule change on April 10, 2000, and April 2000, respectively. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

Nasdaq has filed with the Commission a proposed rule change to

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Letter to Jack Drogin, Senior Special Counsel, Division of Market Regulation, Commission, from Robert E. Aber, Senior Vice President and General Counsel, Nasdaq, dated April 7, 2000 ("Amendment No. 1"). Amendment No. 1 clarifies that the proposed time frame for gaining compliance with the continued inclusion market capitalization standards applies to issuers listed on both the Nasdaq SmallCap Market and the Nasdaq National Market. In addition, Amendment No. 1 clarifies that the method for regaining compliance with the continued inclusion requirement for the number of market makers set forth in Rule 4310(c)(8)(A) applies to issuers listed on both The Nasdaq SmallCap Market and the Nasdaq National Market. Finally, Amendment No. 1 makes certain technical corrections to the proposed rule change.

⁴ See Letter to Jack Drogin, Senior Special Counsel, Division of Market Regulation, Commission, from Robert E. Aber, Senior Vice President and General Counsel, Nasdaq, dated April 25, 2000 ("Amendment No. 2"). Amendment No. 2 clarifies that Rule 4310(c)(8)(C) is being amended to specify time frames for determining when an issuer is non-compliant or has regained compliance with the Association's market capitalization standards. Amendment No. 2 also clarifies that the NASD's Rule 4300 series contains the qualification requirements for all securities included in The Nasdaq Stock Market while the Rule 4400 Series sets forth additional requirements for those securities designated for the Nasdaq National Market.

³⁵ See Securities Exchange Act Release No. 38708 (June 2, 1997), 62 FR 31650 (June 10, 1997) ("1997 Order").

³⁶ See 1997 Order, *supra* note 34. As discussed above, NASD Regulation withdrew proposed NASD Rule 2520(f)(2)(m)(ii) from the proposal.

³⁷ 15 U.S.C. 78s(b)(2).

³⁸ 17 CFR 200.30-3(a)(12).