

proposed rule change prior to the 30th day after publication in the Federal Register.

#### IV. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to the NASD and, in particular, the requirements of Section 15A of the Act and the rules and regulations thereunder. The Commission believes that the proposed rule change will allow the NASD to carry out the purposes of the Act to comply with, and enforce compliance by its members and associated persons, with the provisions of the Act, the rules and regulations thereunder, and the rules of the NASD. Furthermore, the amendments are designed (with amendments to the NASD By-Laws simultaneously approved in SR-NASD-96-20, as set forth below) to assure a fair representation of the NASD's members, in the selection of its directors and administration of its affairs as well as comply with the public and non-industry participant requirements of the Act. It is envisioned that these rules and any subsequent changes that may be implemented from time-to-time will enable the NASD to better comply with the requirements of Section 15A(b)(2) in particular and the Act in general.

The Commission finds good cause for approving the proposed rule change prior to the 30th day after the date of publication of notice of filing thereof in that accelerated approval will enhance the NASD's ability to carry out its regulatory obligations under the Act. The Commission believes that the proposed rule change is intended to accomplish certain allocations and delegations of authority necessary to reorganize the NASD, and establish as separate subsidiaries the NASDR and Nasdaq in accordance with the September 1995 recommendations of The Select Committee on Structure and Governance in order to enable the NASD to meet its regulatory and business obligations. The Plan, which is part of this proposed rule change, sets forth the purpose, functions, governance, procedures, and responsibilities of the NASD, the NASDR and Nasdaq following the reorganization of the NASD. The NASD's Board of Governors, which has been reorganized to be consistent with the proposed rule change, has held meetings to carry out the business of the Association. The subsidiaries also have held meetings of the Board of Directors of NASDR and Nasdaq in order to carry out the business of the subsidiaries

during the 90 day period during which the Plan has been effective.

The proposed rule change, with the exception of the three amendments submitted herein, was previously filed with the Commission in SR-NASD-96-16 and was simultaneously published for comment and approved by the Commission on a temporary basis for a period of 90 days in Release 34-37107. The 90-day approval period expires on July 10, 1996. No comment letters concerning SR-NASD-96-16 were received by the Commission. The reorganization of the NASD Board of Governors is also reflected in proposed rule changes to the NASD By-Laws submitted in rule filing SR-NASD-96-20 and published for comment by the Commission in Securities Exchange Act Release No. 37282 (June 6, 1996), 61 FR 29777 (June 12, 1996). The Commission is granting temporary accelerated approval to that proposed rule change.<sup>7</sup>

Accordingly, the Commission believes that accelerating the approval of the proposed rule change will benefit members and the public interest by fully implementing the reorganization of the NASD and its subsidiaries.

#### V. 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, 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 for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to the file number in the caption above and should be submitted by August 8, 1996.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act, that the proposed rule change SR-NASD-96-29 be, and hereby is, approved for a period of 120 days.

<sup>7</sup> See Securities Exchange Act Release No. 37424 (July 11, 1996).

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

Margaret H. McFarland,

*Deputy Secretary.*

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[Release No. 34-37426; File No. SR-NASD-96-25]

### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc. ("NASD" or "Association") Relating to the Application of the Primary Nasdaq Market Maker Rule to Initial Public Offerings**

July 11, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on June 21, 1996, the National Association of Securities Dealers ("NASD" or "Association") 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 by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The NASD proposes to amend NASD Rule 4612,<sup>2</sup> the NASD's Primary Nasdaq Market Maker Standards Rule ("PMM Rule"), to clarify and codify NASD interpretations with respect to the application of the PMM Rule to initial public offerings ("IPOs"). A more detailed explanation and description of these interpretations will also be provided in a Special Notice-to-Members to be issued contemporaneously with the submission of this filing. Proposed new language is italicized:

#### **NASD Rule 4612 Primary Nasdaq Market Maker Standards**

\* \* \* \* \*

(g)(2) \* \* \*

(B) For initial public offerings (*IPOs*):

(i) the market maker may register in the offering and immediately become a

<sup>8</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> Prior to the revision of the NASD Manual, Rule 4612 was Section 49 of the NASD Rules of Fair Practice.

Primary Nasdaq Market Maker if it is a Primary Nasdaq Market Maker in 80% of the securities in which it has registered; provided, however, that if, at the end of the first review period, the Primary Nasdaq Market Maker has withdrawn on an unexcused basis from the security or has not satisfied the qualification criteria, it shall not be afforded a Primary Nasdaq Market Maker designation on any subsequent initial public offerings for the next 10 business days; or

(ii) the market maker registers in the stock as a regular Nasdaq market maker and satisfies the qualification criteria for the next review period.

(C) For purposes of subparagraph (B)(i) above:

(i) an issue ceases to be an IPO once it has traded on Nasdaq for five (5) business days; and

(ii) the applicable first review period for IPOs that come to market during the last five (5) business days of a month is the calendar month after the month in which the IPO commenced trading on Nasdaq.

\* \* \* \* \*

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

In its filing with the Commission, the NASD included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements and Special Notice-to-Members may be examined at the places specified in Item IV below. The NASD has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

#### 1. Purpose

On June 29, 1994, the SEC approved the NASD's short-sale rule applicable to short sales<sup>3</sup> in the Nasdaq National Market ("NNM").<sup>4</sup> The rule, which has been approved by the Commission on a

pilot basis through August 3, 1996,<sup>5</sup> prohibits member firms from effecting short sales at or below the current inside bid as disseminated by the Nasdaq system whenever that bid is lower than the previous inside bid.<sup>6</sup>

In order to ensure that market maker activities that provide liquidity and continuity to the market are not adversely constrained when the short sale rule is invoked, the rule provides an exemption to "qualified" Nasdaq market makers. Even if a market maker is able to avail itself of the qualified market maker exemption, it can only utilize the exemption from the short sale rule for transactions that are made in connection with *bona fide* market making activity. If a market maker does not satisfy the requirements for a qualified market maker, it can remain a market maker in the Nasdaq system, however, it can not take advantage of the exemption from the rule.

From February 1, 1996 to August 3, 1996, a "qualified" Nasdaq market maker is defined to be a market maker that satisfies the criteria for a PMM found in NASD Rule 4612.<sup>7</sup> To qualify as a PMM, market makers must satisfy at least two of the following three criteria: (1) The market maker must be at the best bid or best offer as shown on the Nasdaq system no less than 35 percent of the time; (2) the market maker must maintain a spread no greater than 102 percent of the average dealer spread; or (3) no more than 50 percent of the market maker's quotation updates may occur without being accompanied by a trade execution of at least one unit of trading. If, however, the market maker satisfies only one of the

<sup>5</sup> See Securities Exchange Act Release No. 36532 (Nov. 30, 1995), 60 FR 62519 (Dec. 6, 1995) (order approving File No. SR-NASD-95-58).

<sup>6</sup> Nasdaq calculates the inside bid and the best bid from all market makers in the security (including bids on behalf of exchanges trading Nasdaq securities on an unlisted trading privileges basis), and disseminates symbols to denote whether the current inside bid is an "up bid" or a "down bid." Specifically, an "up bid" is denoted by a green "up" arrow symbol and a "down bid" is denoted by a red "down" arrow symbol.

Accordingly, absent an exemption from the rule, a member can not effect a short sale at or below the inside bid in a security in its proprietary account or an account of a customer if there is a red arrow next to the security's symbol on the screen. In order to effect a "legal" short sale on a down bid, the short sale must be executed at a price at least a  $\frac{1}{16}$  of a point above the current inside bid. Conversely, if the security's symbol has a green up arrow next to it, members can effect short sales in the security without any restrictions. The rule is in effect during normal domestic market hours (9:30 a.m. to 4:00 p.m., Eastern Standard Time).

<sup>7</sup> Before the PMM standards went into effect, a "qualified market maker" was defined to be a market maker that had entered quotations in the relevant security on an uninterrupted basis for the preceding 20 business days, the so-called "20-day test."

criteria, the market maker may still qualify as a PMM if the market maker executes  $1\frac{1}{2}$  times its "proportionate" volume in the stock.<sup>8</sup> If a market maker is a PMM, a "P" indicator is displayed next to its market maker identification to denote that it is a PMM.<sup>9</sup>

With respect to initial public offerings, the PMM Rule provides that if a member firm has obtained PMM status in 80 percent or more of the stocks in which it has registered ("80 Percent Firm"), the firm may immediately become a PMM in an IPO by registering and entering quotations in the issue.<sup>10</sup> However, if the firm: (1) withdraws from the IPO on an unexcused basis any time during the calendar month in which the IPO commenced trading on Nasdaq or (2) fails to meet the PMM standards for the month in which the IPO commenced trading on Nasdaq, then the entire firm is precluded from becoming a PMM in any other IPO for ten business days following unexcused withdrawal or failure to meet the PMM standards ("10-day penalty rule").<sup>11</sup>

The purpose of the instant rule filing is to amend the PMM Rule to implement and codify two recent NASD interpretations concerning the operation of the PMM Rule in IPO situations. The first amendment reflects that a newly-listed Nasdaq issue ceases to be an IPO once it has traded on Nasdaq for five business days. Thus, if an "80 Percent Firm" registered in a stock on the sixth business day after the issue was first listed on Nasdaq and thereafter withdrew from the stock on an unexcused basis during the calendar month in which the issue commenced trading on Nasdaq, the firm would not be subject to the "10-day penalty

<sup>8</sup> For example, if there are 10 market makers in a stock, each dealer's proportionate share volume would be 10 percent; therefore,  $1\frac{1}{2}$  times proportionate share volume would mean 15 percent of overall volume.

<sup>9</sup> The review period for satisfaction of the PMM performance standards is one calendar month. If a PMM has not satisfied the threshold standards after a particular review period, the PMM designation will be removed commencing on the next business day following notice of failure to comply with the standards. Market makers may requalify for designation as a Primary Market Maker by satisfying the threshold standards for the next review period.

<sup>10</sup> The PMM rule also has provisions applicable to secondary offerings and merger and acquisition situations. See subparagraphs (g)(2)(A) and (g)(3) of NASD Rule 4612.

<sup>11</sup> If a market maker were to register in an IPO as a non-PMM despite the fact that its firm met the 80 Percent Test, then the ten-day penalty rule would not be activated if the market maker were to withdraw from the IPO on an unexcused basis or fail to meet the PMM standards for the issue. Since Nasdaq automatically appends a PMM designation to an "80 Percent Firm" when it registers in an IPO, it is incumbent upon the firm to notify Nasdaq Market Operations when it wishes to trade as a non-PMM in an IPO before it begins quoting the issue.

<sup>3</sup> The term "short sale" refers to a sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller. To determine whether a sale is a short sale, members must adhere to the definition of a "short sale" contained in SEC Rule 3b-3, which rule is incorporated into Nasdaq's short sale rule by NASD Rule 3350(k)(1).

<sup>4</sup> See Securities Exchange Act Release No. 34277 (Jun. 29, 1994), 59 FR 34885 (July 7, 1994) (order approving File No. SR-NASD-92-12).

rule.”<sup>12</sup> The second amendment provides that the applicable first PMM review period for IPOs that come to market during the last five business days of a month is the calendar month after the month in which the IPO commenced trading on Nasdaq. Thus, if an IPO comes to market on the last day of a month, the applicable PMM review period would be the next full calendar month, not the single day on which the issue was first listed on Nasdaq. The NASD believes this amendment is appropriate because it avoids situations where NASD members may be potentially subject to the “ten-day penalty rule” based on just a few days of trading activity.

## 2. Statutory Basis

The NASD believes the proposed rule change is consistent with Section 15A(b)(6) of the Act.<sup>13</sup> Section 15A(b)(6) requires that the rules of a national securities association be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest. Specifically, the NASD believes the proposed rule change will help to ensure the fair and efficient operation and administration of the PMM Rule. The NASD also believes the proposed rule change will help to ensure that NASD members understand the operation of the PMM Rule.

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

The proposed rule change does not 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 Association has neither solicited nor received written comments on the proposed rule change.

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

The foregoing rule change constitutes a stated policy, practice, or

interpretation with respect to the meaning, administration, or enforcement of an existing rule and, therefore, has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>14</sup> and subparagraph (e) of Rule 19b-4 thereunder.<sup>15</sup>

At any time within sixty days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

## 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 at the Commission's Public Reference Room. Copies of such filing also will be available for inspection and copying at the principal office of the National Association of Securities Dealers, Inc. All submissions should refer to File No. SR-NASD-96-25 and should be submitted by August 8, 1996.

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

Margaret H. McFarland,

*Deputy Secretary.*

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[Release No. 34-37428; File No. SR-NYSE-94-34]

## **Self-Regulatory Organizations; Notice of Filing of Amendment No. 3 to Proposed Rule Change by New York Stock Exchange, Inc. Relating to Amendment of Exchange Rule 92**

July 11, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”), 15 U.S.C. § 78s(b)(1), notice is hereby given that on June 28, 1996, the New York Stock Exchange, Inc. (“NYSE” or “Exchange”) 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 by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The proposed rule change consists of further amendments to Rule 92 which would allow member organizations to trade along with customers when liquidating a block position or engaging in arbitrage, subject to certain conditions, and which would limit the circumstances under which Rule 92 would apply to trades by a member or member organization off the Exchange.

The following is the text of the proposed rule change marked to reflect all of the proposed changes to the current rule.<sup>1</sup> Additions to the current rule are in italics and deletions are in brackets.

### **Rule 92: Limitations on Members' Trading Because of Customers' Orders**

[(a) No member shall (1) personally buy or initiate the purchase of any security on the Exchange for his own account or for any account in which he, his member organization or any other member, allied member or approved person, in such organization or officer thereof, is directly or indirectly interested, while such member personally holds or has knowledge that his member organization holds an unexecuted market order to buy such security in the unit of trading for a customer, or (2) personally sell or

<sup>1</sup> The text of the proposed rule change published below incorporates all of the changes to the original rule proposal made in Amendment Nos. 1, 2, and 3. See Securities Exchange Act Release Nos. 35139 (Dec. 22, 1994), 60 FR 156 (Jan. 3, 1995) (notice of filing of proposed rule change, including Amendment No. 1); 36015 (July 21, 1995), 60 FR 38875 (July 28, 1995) (notice of filing of Amendment No. 2).

<sup>12</sup> The market maker, however, would be subject to the 20 day penalty rule. See NASD Rule 4730.

<sup>13</sup> 15 U.S.C. 78o-3(b)(6).

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

<sup>15</sup> 17 CFR 240.19b-4.

<sup>16</sup> 17 CFR 200.30-3(a)(12).