

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39688; File No. SR-NASD-98-16]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change By the National Association of Securities Dealers, Inc. Relating to Peer Review of Auditors of Foreign Issuers Listed on the Nasdaq SmallCap Market

February 20, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on February 18, 1998, the National Association of Securities Dealers, Inc. ("NASD" or "Association") filed with the Securities and Exchange Commission ("Commission") through its wholly owned subsidiary, the Nasdaq Stock Market, Inc. ("Nasdaq"), the proposed rule change as described in Items I and II below, which Items have been prepared by Nasdaq.<sup>2</sup> 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

Nasdaq is proposing a rule change to NASD Rule 4320 ("Rule 4320") to make a technical correction clarifying the application of the peer review requirement to the auditors of foreign issuers and conforming the text of Rule 4320 to the text of Rule 4460. Below is the text of the proposed rule change. Proposed new language is in *italics*.

##### *Rule 4320. Qualification Requirements for Non-Canadian Foreign Securities and American Depositary Receipts*

(a)-(d) No change.

(e) In addition to the requirements contained in paragraphs (a), (b), or (c) and (d), the security shall satisfy the following criteria for inclusion in Nasdaq:

(1)-(2) No change.

(21) Corporate Governance

Requirements—No provisions of this subparagraph or of subparagraph (23) shall be construed to require any foreign issuer to do any act that is contrary to a law, rule or regulation of any public authority exercising jurisdiction over such issuer or that is contrary to

generally accepted business practices in the issuer's country of domicile. Nasdaq shall have the ability to provide exemptions from the applicability of these provisions as may be necessary or appropriate to carry out this intent.

Nasdaq shall review the issuer's past corporate governance activities. This review may include activities taken place while the issuer is listed on Nasdaq or an exchange that imposes corporate governance requirements, as well as activities taking place after the issuer is no longer listed on Nasdaq or an exchange that imposes corporate governance requirements. Based on such review, Nasdaq may take any appropriate action, including placing of restrictions on or additional requirements for listing, or the denial of listing of a security if Nasdaq determines that there have been violations or evasions of such corporate governance standards. Determinations under this subparagraph shall be made on a case-by-case basis as necessary to protect investors and the public interest.

(A)-(H) No change.

(22)-(23) No change.

(f) No change.

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

In its filing with the Commission, Nasdaq 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 may be examined at the places specified in Item IV below. Nasdaq 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*

On August 23, 1997, the SEC approved changes to the listing requirements for the Nasdaq Stock Market. See Release 34-38961 (Aug. 22, 1997), 62 FR 45895 (Aug. 29, 1997). Among the changes approved was the extension of the corporate governance requirements that applied to National Market issuers to the SmallCap Market. In addition, a new corporate governance requirement was added to both the National Market and the SmallCap Market that auditors of Nasdaq listed companies be subject to a practice monitoring program under which the auditor's quality control system would be reviewed by an independent peer

auditor on a periodic basis ("peer review requirement").

In general, a corporate governance requirement does not apply to a foreign issuer if the requirement is contrary to a law, rule or regulation of any public authority exercising jurisdiction over the issuer or is contrary to generally accepted business practices in the issuer's country of domicile. See NASD Rule 4460(a). This provision expressly applies to the new peer review requirement for National Market issuers. However, as a result of the way the revised rules were drafted, the provision could be clarified to more clearly apply to the peer review requirement for Nasdaq SmallCap issuers. This proposed rule change makes that clarification by amending Rule 4320(e)(21) to conform it with Rule 4460, thereby facilitating easier understanding of the rule. In summary, the proposed rule change clarifies that the peer review requirement applies in exactly the same manner for a SmallCap Market issuer as it does for a National Market issuer; a foreign issuer, whether listed on the Nasdaq National Market or The Nasdaq SmallCap Market, is required to be audited by an auditor subject to the peer review requirement to the extent that the requirement is consistent with the generally accepted business practices in the issuer's country of domicile.

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act in that the proposed rule change is 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, and to remove impediments to and perfect the mechanism of a free and open market.

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

Nasdaq does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

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

Written comments were neither solicited nor received.

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

<sup>2</sup> Technical amendments were made to the proposal on the same date. Telephone conversation between Arnold Golub, Office of General Counsel, Nasdaq, and Kenneth Rosen, Attorney, Division of Market Regulation, Commission (February 18, 1998).

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

Nasdaq is filing this proposed rule change as a "non-controversial" rule change under Rule 19b-4(e)(6)<sup>3</sup> because the proposed change: (1) will not significantly affect the protection of investors or the public interest; (2) will not impose any significant burden on competition; and (3) will not become operative for 30 days after the date of this filing, or such shorter time as the Commission may designate. The SEC approved the substance of the change for Nasdaq National Market companies in Release 34-38961<sup>4</sup> and, in so doing, did not find that an exception for foreign issuers would affect impermissibly the protection of investors or the public interest. Similarly, the correction in this proposed rule change should not significantly affect the protection of investors or the public interest. Because the maintenance requirements approved by the SEC in Release 34-38961 will take effect for all issuers on the Nasdaq SmallCap Market on February 23, 1998, Nasdaq requests acceleration of the operative date of this proposed change to February 23, 1998. The Commission finds that it is consistent with the protection of investors and the public interest to permit the proposed rule change to become operative on February 23, 1998.

At any time within 60 days of the filing of the 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, 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, 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 No. SR-NASD-98-16 and should be submitted by March 20, 1998.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>5</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-39693; File No. SR-NSCC-97-13]

### **Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing of Proposed Rule Change Relating to Changes in Membership Standards**

February 23, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on October 30, 1997, the National Securities Clearing Corporation ("NSCC") filed with the Securities and Exchange Commission ("Commission") and on December 31, 1997, amended the proposed rule change as described in Items I, II, and III below, which items have been prepared primarily by NSCC. 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 will amend NSCC's rules regarding membership standards to allow for consideration of applicants' and participants' regulatory history.

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

In its filing with the Commission, NSCC 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 may be examined at the places specified in Item IV below. NSCC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.<sup>2</sup>

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

NSCC believes that when a person with significant managerial responsibility for a firm or who otherwise has significant ability to influence the policies and actions of a firm has a record that fails to reflect a history of good character, citizenship, commercial honor, and a respect for the letter and intent of the legal and regulatory structure in which the firm operates, there is an increased likelihood that the firm will present additional risk to NSCC's participants. Currently NSCC's rules provide that it will establish, as deemed necessary or appropriate, standards of financial responsibility, operational capability, experience, and competence for membership, as well as guidelines for the application of membership standards.<sup>3</sup> The purpose of the proposed rule change is to provide definition to the bases upon which NSCC may take action to deny an applicant membership or to cease to act for a participant by establishing specific membership standards for NSCC applicants and participants.<sup>4</sup>

The revised rule will allow NSCC to deny membership to any applicant or to cease to act for any participant when a person with significant managerial responsibility or with significant ability to influence the policies and actions of the applicant or participant (through ownership interest, contract, or otherwise), whether or not the person

<sup>2</sup> The Commission has modified the text of the summaries prepared by NSCC.

<sup>3</sup> Rule 15 of NSCC's Rules and Procedures.

<sup>4</sup> NSCC has taken note of the findings set forth in the April 15, 1997, memorandum entitled, "The Joint Regulatory Sales Practice Sweep: Heightened Supervisory Procedures," which was the product of an initiative involving the National Association of Securities Dealers, Inc., the New York Stock Exchange, Inc., the Securities and Exchange Commission, and the North American Securities Administrators Association, Inc.

<sup>3</sup> 17 CFR 240.19b-4(e)(6). In reviewing this rule, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. § 78c(f).

<sup>4</sup> SR-NASD-97-16 (Aug. 22, 1997), 62 FR 45895 (Aug. 29, 1997).

<sup>5</sup> 17 CFR 200.30-3(a)(12).

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