

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, 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 at the Commission's Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing also will be available for inspection and copying at the principal office of the Amex. All submissions should refer to File No. SR-Amex-97-16 and should be submitted by April 29, 1997.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>9</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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#### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-38468; File No. SR-NASD-96-46]

#### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by NASD Regulation, Inc. Relating to the Submission of Information in Electronic Form

April 2, 1997.

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 March 17, 1997,<sup>1</sup> NASD Regulation, Inc. ("NASDR") 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 NASDR. 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

NASDR is proposing to amend Rule 8210 of the Procedural Rules of the National Association of Securities Dealers, Inc. ("NASD" or "Association") to permit the NASD to request that members provide regulatory information in electronic form (where the member maintains its records in electronic form) and to establish electronic submission programs for regularly filed regulatory information. Below is the text of the proposed rule change. Proposed new language is in italics.

##### *Procedural Rules*

##### 8000. Complaints, Investigations and Sanctions

\* \* \* \* \*

##### 8200. Investigations

##### 8210. Reports and Inspection of Books for Purpose of Investigating Complaints

(a) For the purpose of any investigation, or determination as to filing a complaint or any hearing of any complaint against any member of the Association or any person associated with a member made or held in accordance with the Rule 9000 Series, or made or held by another domestic or foreign self-regulatory organization, association, securities or contract market or regulator of such markets, with whom the Association has entered into an agreement providing for the exchange of information and other forms of material assistance solely for market surveillance, investigative, enforcement or other regulatory purposes, any District Business Conduct Committee, the Market Surveillance Committee, or the Board of Governors, or any duly authorized member or members of any such Committees or Board or any duly authorized agent or agents of any such Committee or Board shall have the right:

(1) to require any member of the Association, person associated with a member, or person no longer associated with a member when such person is subject to the Association's jurisdiction to report, either informally or on the record, orally or in writing or *electronically (if the requested information is maintained in electronic form)* with regard to any matter involved in any such investigation or hearing, and

(2) to investigate the books, records and accounts of any such member or person with relation to any matter involved in any such investigation or hearing.

(b) No such member or person shall fail to make any report as required in this Rule, or fail to permit any inspection of books, records and accounts as may be validly called for under this Rule. Any notice requiring an *electronic*, oral, or written report or calling for an inspection of books, records and accounts pursuant to this Rule shall be deemed to have been received by the member or person to whom it is directed by the mailing thereof to the last known address of such member or person as reflected on the Association's records.

(c) *In carrying out its responsibilities under this paragraph, the Association may, as approved by the Commission, establish programs for the submission of information to the Association on a regular basis through a direct or indirect electronic interface between the Association and members.*

\* \* \* \* \*

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

In its filing with the Commission, NASDR 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. NASDR 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

(a) Various NASD and SEC rules require members to maintain records of compliance so that information will be available to NASD staff for on-site examination. In addition, members are required by NASD and SEC rules to submit certain information to the NASD on a regular basis or on request. The various rules and regulations of the Municipal Securities Rulemaking Board ("MSRB") also impose recordkeeping requirements on members of the Association. Rule 8210 of the Association's Conduct Rules (formerly, Article IV, Section 5 of the Rules of Fair Practice) requires members to respond to any NASD request for information for the purpose of any investigation or determination as to the filing of a

<sup>9</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> On December 17, 1996, the NASDR filed the proposed rule change with the Commission. However, Amendment No. 1, modifying the rule language, replaces the original rule filing.

complaint or any hearing of a complaint and to submit such information "orally or in writing." This provision covers the Association's request for investigatory information in the context of an individual examination or investigation of a member firm and also covers the Association's programs for the receipt of regular reports from members.

**Amendment to Obtain Information in Electronic Form**—In recent years, members have increasingly maintained their trading records in computer-based technology ("electronic") rather than hard copy form, particularly as the rapidly expanding volume of securities transactions has required the speed of electronic processing. At this time, most members store their primary trading records in some form of electronic storage media.<sup>2</sup> Such electronic storage capability is provided either in-house or through a service bureau. Relatively few members maintain their records only in manual form.

With respect to the Association's conduct of an individual examination or investigation of a member firm's trading activities, the NASD has previously requested such information in hard copy or "written" form, even where the member stored the information in electronic form.<sup>3</sup> In these cases, members provide a hard copy print of the electronically stored data or the examining staff reviews electronic data displayed on-line to transfer the information to hard copy. To the extent that members store their important trading records in electronic storage media, many members have indicated that they prefer that the staff of the NASD accept such trading information in that form because of increased cost efficiencies.<sup>4</sup> The SEC has recently announced policies that clarify when and in what manner members are

permitted to store the books and records required by SEC rules in electronic form.<sup>5</sup> NASDR is, moreover, currently engaged in a long-term initiative that will permit examining staff to utilize current computer-based technology in the course of conducting an examination of a member firm to analyze larger numbers of securities transactions than can be achieved using current manual methodology.<sup>6</sup>

The Association believes that the current provision of Rule 8210 that permits the Association to request that a member or a person associated with a member report "in writing," covers information stored by a member in a form of electronic media, as the electronic format merely retains the written record. The NASDR is, however, proposing to amend Rule 8210 to provide specifically that a member may be required to submit a report in electronic form where the member maintains the information in that manner. The proposed rule change would amend subparagraph (a)(1) to require "\* \* \* any member of the Association, person associated with a member, or person no longer associated with a member when such person is subject to the Association's jurisdiction to report, either informally or on the record, orally or in writing or electronically (if the requested information is maintained in electronic form) with regard to any matter involved in any such investigation or hearing \* \* \*" and would amend subparagraph (b) to insert the word "electronic" in the provision regarding the receipt of any notice requiring a report (emphasis provided). NASDR believes that this action will both increase examination efficiency and will eliminate the costs borne by members in providing electronically maintained information in hard copy to NASDR examiners. Consequently, the potential for human error and delay attendant with paper submission will be decreased.

**Amendment to Establish Electronic Submission Programs**—The NASD has also worked with the membership over many years to develop procedures for the electronic submission of periodic reports or other frequently requested investigatory data that would otherwise be submitted in written form in order to better fulfill its regulatory responsibilities under the federal

securities laws. Such programs for electronic submissions have already been established for filing of members' FOCUS Reports, Blue Sheet Reports, Short Interest Reports, Forms U-4 and U-5 with Central Registration Depository ("CRD").<sup>7</sup>

As the Association continues to increase its services to the membership and enhance its ability to surveil for regulatory compliance through the use of computer-based technology, it is important that NASDR be able to establish electronic submission programs for information required to be submitted by members on a regular basis. In recent discussions with the membership on this issue, members indicated they preferred to submit frequently filed information electronically because of assurance of receipt (in comparison to the mails) and the ability to amend a previously-submitted filing if an error is subsequently discovered. The Association is, therefore, proposing to amend Rule 8210 to add new paragraph (c) to provide general authority for the Association to establish programs for the submission of information on a regular basis through direct or indirect electronic interface between the Association and members, upon approval by the Commission.

(b) The NASD believes that the proposed rule change is consistent with the provisions of Sections 15A(b)(6),<sup>8</sup> and 15A(b)(7),<sup>9</sup> of the Act.<sup>10</sup> The proposed rule change will permit the NASD to request that members provide regulatory information in electronic form (where the member maintains its records in electronic form) and to establish electronic submission programs for regularly filed regulatory information, upon Commission approval. The proposed rule will also assist the Association in preventing

<sup>2</sup> The Association's findings are based on technology surveys conducted of the membership in connection with establishing electronic submission programs with respect to the filing of FOCUS Reports, Blue Sheet Reports, Short Interest Reports, Forms U-4 and U-5, and Free-Riding and Withholding Questionnaires, which electronic submission programs are more fully discussed below.

<sup>3</sup> Submission of information "orally," as permitted by the Interpretation, is generally limited to situations where Association staff engage in a conversation with the member and information is elicited from the member in the course of the conversation.

<sup>4</sup> Providing an electronic copy of part or all of electronically stored information is less costly to the member in terms of personnel time and computer time than providing a hard copy printout or arranging for examining staff to review information on-line. The cost and time-saving advantages for broker-dealers of storing information in electronic media is recognized by the Commission in Securities Exchange Act Release No. 38245, Feb. 5, 1997; 62 FR 6469, Feb. 12, 1997.

<sup>5</sup> See, Securities Exchange Act Release No. 38245, Feb. 5, 1997; 62 FR 6469, Feb. 12, 1997.

<sup>6</sup> See, advice to the SEC regarding the electronic program for the Free-Riding and Withholding Questionnaire in correspondence dated March 1, and August 2, 1996 and announced in Notice to Members 96-18 (March 1996).

<sup>7</sup> The FOCUS Filing Plan was approved in Securities Exchange Act Rel. No. 29105 (April 18, 1991); 56 FR 19131 (April 25, 1991). The Short Interest Reporting requirement was permanently approved in Securities Exchange Act Rel. No. 23482 (July 30, 1986); 51 FR 28472 (Aug. 7, 1986). The Blue Sheet Reporting Plan was approved in Securities Exchange Act Rel. No. 26539 (Feb. 13, 1989); 54 FR 7318 (Feb. 17, 1989). The Central Registration Depository electronic filing requirements were approved in Securities Exchange Act Rel. No. 37439 (July 15, 1996); 61 FR 37950 (July 22, 1996).

<sup>8</sup> Section 15A(b)(6) requires the Association to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade and to protect investors and the public interest.

<sup>9</sup> Section 15A(b)(7) requires that the rules of the Association provide that its members and persons associated with its members shall be appropriately disciplined for violation of the rules of the MSRB or the rules of the Association.

<sup>10</sup> 15 U.S.C. § 78o-3.

fraudulent and manipulative acts and practices, in promoting just and equitable principles of trade, in protecting investors and the public interest, and in appropriately disciplining members for violations of its rules, the rules and regulations of the Commission, and the rules of the MSRB.

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

The NASD 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.

*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.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) As the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- A. by order approve such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

**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. 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 April 29, 1997.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

**Margaret H. McFarland,**

*Deputy Secretary.*

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**SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-38462; File No. SR-PSE-96-45]

**Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Pacific Stock Exchange Incorporated Relating to the Exchange's Lead Market Maker Options Book Pilot Program**

April 1, 1997.

**I. Introduction**

On December 10, 1996, the Pacific Stock Exchange Incorporated ("PSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder<sup>2</sup> a proposal to expand the scope of its Lead Market Maker ("LMM") Book Pilot Program to allow additional LMMs to participate and to allow a greater number of option issues to be eligible under the program. The proposal was published for comment in the **Federal Register** on February 19, 1997.<sup>3</sup> No comments were received on the proposal. This order approves the Exchange's proposal.

**II. Description of the Proposal**

On October 11, 1996, the Commission approved an Exchange proposal to adopt a one-year pilot program under which some LMMs are permitted to manage the options public limit order book ("Book") in certain designated issues.<sup>4</sup> Under the pilot, the approved LMMs manage the Book function, take responsibility for trading disputes and errors, set rates for Book execution, and pay the Exchange a fee for systems and services.<sup>5</sup> The program allows LMMs to

have greater control over their operations on the Exchange floor by allowing them, among other things, to set their own rates for execution services provided to customers.

Under the pilot as approved by the Commission, the program is limited to no more than three LMMs and no more than forty option symbols in total,<sup>6</sup> during a one-year pilot phase. The PSE is proposing to expand the scope of the program to allow additional LMMs to participate, and to allow a greater number of option issues to be eligible under the Program. Specifically, the Exchange proposed an expansion of the Book Pilot Program to allow for up to nine LMMs and up to 150 options symbols.

The LMMs who participate during the pilot phase are selected by the Options Floor Trading Committee based on certain designated factors.<sup>7</sup> Approved LMMs must maintain "minimum net capital," as provided in Rule 15c3-1 under the Act,<sup>8</sup> and also must maintain a cash or liquid asset position of at least \$500,000, plus \$25,000 for each issue over five issues for which they perform the function of an OBO. Only multiply-traded option issues are eligible during the pilot phase.

**III. Discussion**

After careful consideration, the Commission finds that the Exchange's proposal to expand the Book Pilot Program is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange in that the proposal is consistent with Section 6(b) of the Act,<sup>9</sup> in general, and Section 6(b)(5),<sup>10</sup> in particular, in that it is designed to facilitate transactions in securities, to promote just and equitable

6.59. In that regard, the Exchange will allow the LMM to utilize Exchange personnel to assist the LMM in performing the OBO function, and the Exchange will charge the LMM a reasonable fee for such use of Exchange personnel. If the program is made permanent, LMMs would be responsible for hiring and maintaining their own employees, but the Exchange would provide employees to assist LMMs when necessary due to market conditions. In all cases, however, employees working in the Book operation will be subject to all rules, policies, and procedures established by the Exchange. With regard to their duties as market makers, LMMs would be required to perform all obligations provided in Rules 6.35 through 6.40 and 6.82.

<sup>6</sup> Each option issue typically has only one symbol associated with it, unless LEAPs are traded on that issue, in which case there usually would be two additional symbols related to the issue, or unless a contract adjustment is necessary due, for example, to a merger or stock split, in which case one additional symbol usually would be added.

<sup>7</sup> See Pilot Approval Order, *supra* note 4.

<sup>8</sup> 17 CFR 240.15c3-1.

<sup>9</sup> 15 U.S.C. § 78f(b).

<sup>10</sup> 15 U.S.C. § 78f(b)(5).

<sup>1</sup> 15 U.S.C. § 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Securities Exchange Act Release No. 38273 (February 12, 1997), 62 FR 7489.

<sup>4</sup> See Securities Exchange Act Release No. 37810 (October 11, 1996), 61 FR 54481 ("Pilot Approval Order").

<sup>5</sup> More specifically, under the rule changes approved by the Commission, LMMs may perform all functions of the Order Book Official ("OBO") in designated issues pursuant to Rules 6.51 through