

because Nasdaq recognizes that executing parties provide significant liquidity to the market on a regular and continuous basis. This liquidity, represented by the maintenance of executable quotes accessible through directed SelectNet orders, is of substantial benefit to all market participants. Nasdaq strongly believes that the continued provision of such liquidity should be encouraged and that the elimination of charges on directed order executions obtained through SelectNet is a way to help achieve that goal.

Nasdaq notes that under the Order Execution Rules, any party may have its trading interest reflected in a quotation displayed for possible execution by an incoming directed order. For example, a customer's limit order that improves a market maker's price must now be displayed in that market maker's quote. Under Nasdaq's proposal, it is conceivable that customer limit orders, and the market liquidity they represent, may be handled by market makers at a lower cost than was the case under the old fee structure. Likewise, Nasdaq market makers who maintain executable quotes will also incur no fees when providing liquidity by having their quotes accessed for execution by others through directed SelectNet orders. Moreover, broker-dealers that enter directed orders seeking to access liquidity will also have their fees significantly reduced for any executions they obtain through SelectNet. These fees are also equally applied, with all market participants being charged the same \$1.00 directed order entry fee. In sum, these fee reductions should result in lower overall transaction costs for all SelectNet system users.

While the new fees start February 1, 1998, Nasdaq believes that a 90-day trial period, commencing the date Nasdaq's new SelectNet fees are published in the **Federal Register**, is appropriate due to uncertainty regarding SelectNet usage levels as a result of the fee changes. Nasdaq will continue to monitor usage levels and trading behavior with a view to future modification of SelectNet charges if warranted.

For the reason set forth above, Nasdaq believes that the proposed rule change is consistent with Section 15A(b)(5) of the Act, which requires that the rules of the NASD provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system which the NASD operates or controls.

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

The NASD believes that the proposed rule change will not 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

Comments were neither solicited nor received.

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

This filing applies to the assessment of SelectNet fees to NASD members, and thus the proposed rule change is effective immediately upon filing pursuant to Section 19(b)(3)(A)(ii) of the Act and subparagraph (e)(2) of Securities Exchange Act Rule 19b-4 thereunder⁵ because the proposal is establishing or changing a due, fee or other charge. At any time within 60 days 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.⁶

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room.

Copies of such filing will also be available for inspection and copying at

⁵ 15 U.S.C. § 78(b)(3)(A)(ii).

⁶ In reviewing the proposal, the Commission has considered the proposal's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

the principal office of the NASD. All submissions should refer to File No. SR-NASD-98-06 and should be submitted by March 11, 1998.

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

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39637; File No. SR-NASD-98-05]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc., Relating to Modifications to the Small Order Execution System

February 10, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on January 28, 1998, the National Association of Securities Dealers, Inc. ("NASD" or "Association") filed with the Securities and Exchange Commission ("Commission") through its wholly owned subsidiary, Nadsaq Stock Market, Inc. ("Nasdaq"), the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. Nasdaq has designated this proposal as one that effects a change in an existing order-entry or trading system of a self-regulatory organization under Section 19(b)(3)(A) of the Act and Rule 19b-4(e)(5) thereunder, which renders the rule effective upon the Commission's receipt of this filing. 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 to amend Rule 4730(b)(10) to address problems associated with the rejection of orders in the Small Order Execution System ("SOES") when there is no market maker at the inside quote. Below is the text of the proposed rule change. Proposed new language is in italics; there are no deletions.

4730. Participant Obligations is SOES

(a) No Change.

⁷ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

(b) Market Makers.

(1)-(9) No Change.

(10) In the event that there are no SOES market makers at the best bid (offer) disseminated by Nasdaq, market orders to sell (buy) entered into SOES will be *held in queue until executable, or until 90 seconds has elapsed, after which such orders will be rejected and returned to their respective order entry firms.*

(c) No Change.

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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 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. The 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

When the SEC Order Handling Rules were implemented in January of 1997, Nasdaq modified the SOES execution process to reject orders back to the entering firm when an electronic communications network ("ECN") or an unlisted trading privilege ("UTP") participant was alone creating the Nasdaq inside quote in a Nasdaq National Market security.² This was necessary because ECNs were unable, at the time, to participate in an automatic execution system such as SOES. ECNs asserted that to do so might expose them to the risk of double executions, because if an order available through an ECN is also accessible through SOES, it may be subject to two executions: one from within the ECN and another from market participants using SOES. This in turn could cause the ECN to take a principal position, which is inconsistent with the ECN's role of acting solely as agent on behalf of its customers.

This has resulted in an unintended consequence, however, which has caused significant concern. Specifically, an ECN quote that effectively halts executions in SOES for a security also allows the ECN customer entering that order to essentially control the inside

price and potentially create an advantage in SOES for this customer (or other customers using SOES) by jumping ahead of other SOES orders that might have executed first in that issue if they had not been rejected. This has become problematic because instances have been observed where the ECN changes its quote almost immediately, before it can be assessed through either SelectNet or its own internal system. Once this quote disappears and a new dealer inside has been established, new SOES orders enter the system which then execute as the first order against the first market maker at the new inside price.

Nasdaq plans to implement the following solutions to this potential problem. When an ECN or UTP participant is alone at the inside in a Nasdaq National Market security, executable SOES orders that are in queue or received at that moment will be held for a specified period of time. This "hold time," initially set at 90 seconds, is the maximum life of an order. Holding the queued orders for 90 seconds will give other market makers time to adjust their quotes to create a new inside, join the ECN at their price, or allow the ECN to move away from the inside. If one of these conditions is met and the order is still executable, it will execute. If any of these conditions do not occur, however, the order will time out, under normal time-out processing, and be returned to the entering firm at the end of the 90-second maximum life of the order. Nasdaq SmallCap securities will continue to execute against the next available SOES market maker at the ECN price.

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) and 15A(b)(11) of the Act³ in that it would facilitate the more orderly and equitable processing of customer orders entered into SOES, and eliminates the potential for participants to intentionally or unintentionally create an advantage among participants who access SOES.

Section 15A(b)(6) requires that the rules of a registered national securities association are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principals 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; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

Section 15A(b)(1) requires that the rules of a registered national securities association be designed to produce fair and informative quotations, prevent fictitious or misleading quotations and to promote orderly procedures for collecting, distributing, and publishing quotations.

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.

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

The rule change has become effective pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(e)(5) thereunder,⁴ because the foregoing proposed rule change effects a change in an existing order-entry or trading system of a self-regulatory organization that:

(1) does not significantly affect the protection of investors or the public interest, (2) does not impose any significant burden on competition, and (3) does not have the effect of limiting the access to or availability of the order-entry or trading system. In particular, investors and the public should benefit as the appropriate priority of SOES orders will be preserved, placing competitors on a more level playing field and protecting their access to the order-entry system.⁵ Notwithstanding that this rule change is effective immediately upon filing, Nasdaq will nonetheless delay implementation of the proposed rule change until at least February 23, 1998, and at least 7 days after notice of such rule change on the Nasdaq Trader Web Site.⁶ Nasdaq will provide notice to market participants of the exact date of implementation prior to the effective date. At any time within 60 days of the filing of such rule change, the Commission may summarily

⁴ 17 CFR 240.19b-4(e)(5).

⁵ 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).

⁶ <http://www.nasdaqtrader.com>.

² See Exchange Act Release No. 38156 (January 10, 1997) 62 FR 2415 (January 16, 1997) (order partially approving File No. SR-NASD-96-43).

³ 15 U.S.C. 78o-3(b)(6) and (b)(11).

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 forgoing, 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 NASDAQ. All submissions should refer to File No. SR-NASD-98-05 and should be submitted by March 11, 1998.

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

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39634; File No. SR-NYSE-94-34]

Self-Regulatory Organizations; Notice of Filing of Amendment No. 4 to Proposed Rule Change by the New York Stock Exchange, Inc. Relating to Exchange Rule 92, "Limitations on Members' Trading Because of Customers' Orders"

February 9, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on December 15, 1997, 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 Exchange. 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

In its original form, the proposed rule change extended the applicability of Exchange Rule 92 to trades by a member or member organization on any market center and provided a limited exemption to permit member organizations to trade along with their customers when liquidating a block facilitation position or engaging in bona fide or risk arbitrage. Amendment No. 4 provides an additional limited exemption for hedging a facilitation position, as well as explanations of the manner in which the amended rule will operate.

The following is the text of the proposed rule change marked to reflect all of the proposed changes.² Additions to the current text of Exchange Rule 92 appear in italics while deletions appear 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 initiate the sale of any security on the Exchange for any such account, while he personally holds or has knowledge

that his member organization holds an unexecuted market order to sell such security in the unit of trading for a customer.

(b) No member shall (1) personally buy or initiate the purchase of any security on the Exchange for any such account, at or below the price at which he personally holds or has knowledge that his member organization holds an unexecuted limited price order to buy such security in the unit of trading for a customer, or (2) personally sell or initiate the sale of any security on the Exchange for any such account at or above the price at which he personally holds or has knowledge that his member organization holds an unexecuted limited price order to sell such security in the unit of trading for a customer.]

(a) *Except as provided in this Rule, no member or member organization shall cause the entry of an order to buy (sell) any Exchange-listed security on the Exchange or any other market center for any account in which such member or member organization or any approved person thereof is directly or indirectly interested (a "proprietary order"), if the person responsible for the entry of such order has knowledge of any particular unexecuted customer's order to buy (sell) such security which could be executed at the same price.*

(b) *A member or member organization may enter an proprietary order while representing a customer order which could be executed at the same price, provided the customer's order is not for the account of an individual investor, and the customer has given express permission, including and understanding of the relative price and sized of allocated execution reports, under the following conditions:*

(1) *the member or member organization is liquidating a position held in a proprietary facilitation account, and the customer's order is for 10,000 shares or more; or*

(2) *the member or member organization is creating a bona fide hedge and (i) the risk to be hedged is the result of a previously-established position, recorded as acquired in the course of facilitating a customer's order; (ii) the size of the offsetting hedging order is commensurate with such risk; and (iii) the customer's order is for 10,000 shares or more; or*

(3) *the member or member organization is engaging in bona fide arbitrage or risk arbitrage transactions, and recording such transactions in an account used solely to record arbitrage transactions (an "arbitrage account").*

(c) The provisions of this Rule shall not apply to:

² The text of the proposed rule change incorporates all of the proposed changes made to the original rule proposal by Amendment Nos. 1, 2, 3, and 4. 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); 37428 (July 11, 1996), 61 FR 37523 (July 18, 1996) (notice of filing of Amendment No. 3). On January 20, 1998, the Exchange submitted a technical correction to Amendment No. 4 to better identify the cumulative proposed changes to Exchange Rule 92. See Letter from Betsy Lampert Minkin, Regulatory Development Project Manager, Exchange, to Michael Loftus, Attorney, Division of Market Regulation, Commission, dated January 12, 1998.

⁷ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).