

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-45990; File No. SR-NASD-00-76]

### Self-Regulatory Organizations; Order Approving a Proposed Rule Change and Amendment Nos. 1, 2, and 3 Thereto by the National Association of Securities Dealers, Inc. Relating to Locked and Crossed Markets That Occur at or Prior to the Market Open

May 28, 2002.

#### I. Introduction

On January 5, 2001, the National Association of Securities Dealers, Inc. ("NASD" or "Association"), through its subsidiary, the Nasdaq Stock Market, Inc. ("Nasdaq"), filed with the Securities and Exchange Commission ("SEC" or "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 proposed rule change to amend the provisions of NASD Rule 4613(e)(1)(C), "Locked and Crossed Markets," to revise the use of Trade-or-Move Messages during locked and crossed market conditions that occur prior to the market's opening, and to add provisions relating to the use of Trade-or-Move Messages prior to the market's close. On January 22, 2001, the NASD, through Nasdaq, filed Amendment No. 1 to the proposed rule change.<sup>3</sup> The proposed rule change and Amendment No. 1 were published for comment in the *Federal Register* on February 7, 2001.<sup>4</sup> The Commission received seven comment letters regarding the proposal.<sup>5</sup> Nasdaq

responded to the commenters in Amendment Nos. 2 and 3 to the proposal, which the NASD, through Nasdaq, filed with the Commission on August 13, 2001,<sup>6</sup> and February 21, 2002,<sup>7</sup> respectively. Amendment Nos. 2 and 3 were published for comment in the *Federal Register* on March 11, 2002.<sup>8</sup> The Commission received three comment letters regarding Amendment Nos. 2 and 3.<sup>9</sup> The NASD, through Nasdaq, responded to the comments regarding Amendment Nos. 2 and 3 on April 5, 2002,<sup>10</sup> and on April 16, 2002,<sup>11</sup>

Trading Issues Committee, STA, to Jonathan G. Katz, Secretary, Commission, dated March 13, 2001 ("STA Letter"); letter from Kevin J.P. O'Hara, General Counsel, Archipelago, L.L.C. ("Archipelago") to Jonathan G. Katz, Secretary, Commission, dated April 3, 2001 ("Archipelago Letter"); and letter from William O'Brien, Senior Vice President & General Counsel, The BRUT ECN, L.L.C., ("BRUT") to the Commission, dated April 17, 2001 ("BRUT Letter").

<sup>6</sup> See letter (with attachment) from Eugene A. Lopez, Senior Vice President, Nasdaq, to Belinda Blaine, Associate Director, Division, Commission, dated August 10, 2001 ("Amendment No. 2"). In Amendment No. 2, Nasdaq responds to the commenters and proposes to revise its original proposal to: (1) require electronic communications networks ("ECNs") to send Trade-or-Move Messages prior to entering locking or crossing quotes and require market makers to send Trade-or-Move Messages after entering locking or crossing quotes; (2) reduce the time to respond to a Trade-or-Move Message to 10 seconds; (3) provide a 10,000-share minimum share requirement for Trade-or-Move Messages for Nasdaq 100 and S&P 400 issues; (4) prohibit all market participants from entering locking or crossing quotes between 9:29:30 a.m. and 9:29:59 a.m.; and (5) delete provisions imposing Trade-or-Move requirements between 3:50 p.m. and 4 p.m.

<sup>7</sup> See letter from Jeffrey S. Davis, Nasdaq, to John Polise, Senior Special Counsel, Division, Commission, dated February 21, 2002 ("Amendment No. 3"). In Amendment No. 3, Nasdaq responds to comments from BRUT and clarifies a misstatement in Amendment No. 2. Specifically, Amendment No. 3 states that the requirement that ECNs send Trade-or-Move Messages prior to entering locking or crossing quotes applies to all orders that ECNs receive and is not limited to agency orders, as stated incorrectly in Amendment No. 2.

<sup>8</sup> See Securities Exchange Act Release No. 45508 (March 5, 2002), 67 FR 10956 ("March 11 Release").

<sup>9</sup> See letter from Joshua Levine to *rule-comments@sec.gov*, Commission, dated April 1, 2002 ("Levine Letter"); letter from Keith Brickman, Managing Director, Morgan Stanley, Inc. ("Morgan Stanley"), to Jonathan G. Katz, Secretary, Commission, dated April 4, 2002 ("Morgan Stanley Letter"); and letter from Chris Holter, Head of OTC Trading, and Betsy Prout Lefler, Director, Equity Capital Markets Compliance, First Union Securities, Inc. ("First Union"), to Commission, dated April 5, 2002 ("First Union Letter").

<sup>10</sup> See letter from Jeffrey S. Davis, Associate General Counsel, Nasdaq, to Yvonne Fraticelli, Special Counsel, Division, Commission, dated April 5, 2002 ("April 5 Letter"). In the April 5 Letter, Nasdaq states its reasons for retaining the Trade-or-Move requirements rather than requiring market participants to enter firm quotes prior to the market opening, as the commenter suggests.

<sup>11</sup> See letter from Jeffrey S. Davis, Associate General Counsel, Nasdaq, to Yvonne Fraticelli, Special Counsel, Division, Commission, dated April

respectively. This order approves the proposed rule change and Amendment Nos. 1, 2, and 3.

#### II. Description of the Proposed Rule Change

##### A. Background

In its original rule proposal, Nasdaq proposed amendments to NASD Rule 4613(e)(1)(C) that would alter the obligations of market makers and ECNs during locked and crossed markets that occur prior to the market's open and also prior to the close. Specifically, Nasdaq originally proposed to: (1) Extend the application of NASD Rule 4613(e)(1)(C)(ii) regarding locked and crossed markets before the open to the period prior to the close; (2) require market makers and ECNs that send a Trade-or-Move Message to do so at least 15 seconds before entering a locking or crossing quote rather than after entering a locking or crossing quote, as the rule currently requires; (3) increase from 5,000 to 10,000 the minimum number of shares that must accompany a non-agency Trade-or-Move Message; and (4) reduce the amount of time within which the recipient of a Trade-or-Move Message must properly respond to the message from 30 seconds to 15 seconds.

The Commission received seven comment letters regarding the original proposal, as amended by Amendment No. 1.<sup>12</sup> In response to the commenters, Nasdaq filed Amendment No. 2 to the proposal, which made several changes to the original proposal to address concerns raised by the commenters. The proposal, as amended by Amendment No. 2, will: (1) Require ECNs to send Trade-or-Move Messages prior to entering locking or crossing quotes and require market makers to send Trade-or-Move Messages after entering locking or crossing quotes; (2) reduce the time to respond to a Trade-or-Move Message to 10 seconds; (3) provide a 10,000-share minimum share requirement for Trade-or-Move Messages for Nasdaq 100 Index ("Nasdaq 100") and S&P 400 Index ("S&P 400") issues; (4) prohibit all market participants from entering locking or crossing quotes between 9:29:30 a.m. and 9:29:59 a.m.; and (5) delete provisions in the original proposal imposing Trade-or-Move requirements between 3:50 p.m. and 4:00 p.m.<sup>13</sup>

15, 2002 ("April 15 Letter"). As discussed more fully below, in the April 15 Letter, Nasdaq addressed concerns raised in the Morgan Stanley Letter and First Union Letter.

<sup>12</sup> See *supra* note 5.

<sup>13</sup> See Amendment No. 2, *supra* note 6.

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

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

<sup>3</sup> See Letter from Jeffrey S. Davis, Assistant General Counsel, Nasdaq, to Sapna C. Patel, Attorney, Division of Market Regulation ("Division"), Commission, dated January 19, 2001 ("Amendment No. 1"). In Amendment No. 1, Nasdaq made a minor technical correction to the rule text.

<sup>4</sup> See Securities Exchange Act Release No. 43913 (January 31, 2001), 66 FR 9394.

<sup>5</sup> See letter from Mark R. Grewe, Managing Director, NDB Capital Markets, L.P., to Jonathan G. Katz, Secretary, Commission, dated February 27, 2001 ("NDB Letter"); letter from Martin Cunningham, Senior Vice President Trading, Schwab Capital Markets L.P. ("Schwab"), to Jonathan G. Katz, Secretary, Commission, dated February 28, 2001 ("Schwab Letter"); letter from Richard B. Levin, Assistant General Counsel and Regulatory Affairs Officer, Knight Securities, L.P. ("Knight"), to the Commission, dated March 1, 2001 ("Knight Letter"); letter from Kim Bang, President, Bloomberg Tradebook LLC ("Bloomberg"), to the Commission, dated March 15, 2001 ("Bloomberg Letter"); letter from Timothy G. Grazioso, Subcommittee Chairman, Trading Issues Committee, Security Traders Association ("STA"), Michael T. Bird, Chairman, Trading Issues Committee, STA, and Geoffrey W. Cloud, Counsel,

## B. Nasdaq's Amended Proposal

### 1. Sequence of Messages

In its original proposal, Nasdaq proposed to revise NASD Rule 4613(e)(1)(C) to require all market participants to send Trade-or-Move Messages before, rather than after, entering a locking or crossing quotation. In response to concerns raised by commenters,<sup>14</sup> Nasdaq revised its proposal to permit the sequence of Trade-or-Move Messages to differ by market participant business model. Specifically, under the amended proposal, ECNs will send a Trade-or-Move Message before entering a locking or crossing quote, and market makers will send a Trade-or-Move Message immediately after entering a locking or crossing quote.<sup>15</sup> Nasdaq believes that the proposed change will permit ECNs to participate more effectively in the pre-opening period, while permitting market makers to retain their current automated systems.<sup>16</sup> Nasdaq believes that the proposed change also will preserve the benefits that Nasdaq sought to achieve when it first implemented the Trade-or-Move requirements, including increased price discovery and decreased gamesmanship surrounding the occurrence and resolution of locked and crossed markets.<sup>17</sup>

### 2. Response Time

Under current NASD Rule 4613(e)(1)(C), the recipient of a Trade-or-Move Message must respond properly to the message within 30 seconds. In the original proposal, Nasdaq proposed to reduce the response time to 15 seconds to reduce the duration of locked and crossed markets that occur.

Based upon commenters' concern that 15 seconds was too long a response time,<sup>18</sup> Nasdaq proposed to reduce the time for responding to a Trade-or-Move Message to 10 seconds. Although Nasdaq acknowledges that this is a relatively brief period for non-automated participants, Nasdaq believes

that firms that choose to participate in the pre-open must vigilantly monitor their quotes.<sup>19</sup> In addition, as described more fully below, Nasdaq believes that the 10-second response time will help ECNs to avoid dual liability.<sup>20</sup>

### 3. Number of Shares

Under current NASD Rule 4613(e)(1)(C), the aggregate size of the Trade-or-Move Message must be at least 5,000 shares (*i.e.*, the market participant must send a total of 5,000 shares to all parties it is locking or crossing) in the case of a proprietary quote, or the actual size of an agency order if that is the basis for the locking or crossing quote. Under the original proposal, Nasdaq sought to raise the minimum Trade-or-Move Message share requirement to 10,000 shares or the actual size of an agency order. Nasdaq believes that a market participant must be willing to risk significant capital and to trade a significant amount if it wishes to lock or cross the market during the ten minutes prior to the opening.

In light of concerns raised regarding the 10,000-share requirement,<sup>21</sup> Nasdaq revised the proposal to limit the 10,000-share Trade-or-Move Message requirement size to proprietary orders involving securities in the Nasdaq 100 Index and the S&P 400 Index. The minimum Trade-or-Move Message size requirement will remain at 5,000 shares for other issues. The "agency exception" contained in current NASD Rule 4613(e)(1)(C) will continue to operate as it does today. Nasdaq believes that Nasdaq 100 and S&P 400 issues are marked by higher liquidity and faster trading and, therefore, merit a more stringent effort to avoid locked or crossed markets. Nasdaq believes that the 10,000-share requirement proportionately increases the economic significance of entering a locking or crossing quotation for stocks that are widely followed and for which a locked or crossed market would have the greatest impact.

### 4. Limited Prohibition on Entry of Locking and Crossing Quotes

Based upon the recommendation of the Trade-or-Move Subcommittee ("Subcommittee") of Nasdaq's Quality of Markets Committee, Nasdaq revised the proposal to prohibit market participants from entering a locking or crossing quote between 9:29:30 a.m. and

9:29:59 a.m.<sup>22</sup> During that period, all market participants will be permitted to send Trade-or-Move Messages for the required number of shares to parties that they would lock or cross if permitted to enter such locking or crossing quotes. Market participants that receive Trade-or-Move Messages during that time period will be obligated to respond properly by trading in full or moving their quote within the appropriate response time.

Nasdaq believes that a prohibition on the entry of locking and crossing quotes immediately prior to the market opening, in conjunction with the continued obligation to respond properly to Trade-or-Move Messages, will facilitate the resolution of locks and crosses that exist at 9:29:30 a.m. Further, Nasdaq believes that the potential benefits to all market participants of a more orderly opening outweigh the limited loss of price discovery that will result from suppressing locking and crossing quotes during that brief but critical period.

### 5. Pre-Closing

Based upon the positive effect that the Trade-or-Move requirements have had on resolving potential locked and crossed markets at and immediately before the market opening, Nasdaq originally proposed to expand the application of NASD Rule 4613(e)(1)(C) to include the 10-minute period preceding the market close (3:50 p.m. to 3:59:59 p.m.). The commenters generally opposed this provision of the original proposal. In light of the comments received and with the implementation of SuperSOES, Nasdaq revised the proposal to eliminate the provisions expanding the application of NASD Rule 4613(e)(1)(C) to the period prior to the closing.

## III. Summary of Comments and Nasdaq's Response

### A. Comments to the Original Proposal and Amendment No. 1

As noted above, the Commission received seven comment letters regarding the original proposal, as amended by Amendment No. 1.<sup>23</sup> In response to the commenters, Nasdaq filed Amendment No. 2 to the proposal, which made several changes to the original proposal to address concerns raised by the commenters. In addition, Nasdaq filed Amendment No. 3 to the

<sup>14</sup> See, e.g., Schwab Letter, *supra* note 5 (asserting that the proposal to require market makers to send a Trade-or-Move Message prior to entering a locking or crossing quote would necessitate manual, rather than automated processing; and NDB Letter, *supra* note 5 (stating that the proposal to require market makers to send a Trade-or-Move Message prior to entering a locking or crossing quote would require substantial programming changes).

<sup>15</sup> "Immediate" issuance of a Trade-or-Move Message will be understood to mean instantaneous in the case of automated systems and not exceeding a different, specified period where manual processes are utilized.

<sup>16</sup> See Amendment No. 2, *supra* note 6.

<sup>17</sup> See Amendment No. 2, *supra* note 6.

<sup>18</sup> See, e.g., Knight Letter and STA Letter, *supra* note 5.

<sup>19</sup> See Amendment No. 2, *supra* note 6.

<sup>20</sup> See Amendment No. 2, *supra* note 6.

<sup>21</sup> See, e.g., Knight Letter, *supra* note 5 (expressing concern that the 10,000-share requirement could require a firm to commit \$1 million to execute an order in certain stocks at a time when the market is not fully functional).

<sup>22</sup> Nasdaq formed the Subcommittee to respond to concerns raised by the initial seven commenters to the proposal. The Subcommittee was comprised of the initial seven commenters and members representing other constituencies within the Nasdaq market making community.

<sup>23</sup> See *supra* note 5.

proposal, which responded to the concerns of one commenter and corrected a misstatement in Amendment No. 2.<sup>24</sup> Amendment Nos. 2 and 3 were published for comment in the March 11 Release.<sup>25</sup> The comments raised by the seven commenters to the original proposal, and Nasdaq's response to the commenters, are discussed in detail in the March 11 Release.

#### *B. Comments Regarding Amendment Nos. 2 and 3 and Nasdaq's Response*

The Commission received three comment letters regarding Amendment Nos. 2 and 3.<sup>26</sup> One commenter suggested that Nasdaq replace the Trade-or-Move requirements with a requirement that market participants enter firm quotes prior to the market open.<sup>27</sup>

In its response, Nasdaq stated that the Subcommittee considered the commenter's suggested approach twice in 2001.<sup>28</sup> Nasdaq believes, however, that the commenter's suggested approach would either shift occurrences of locked and crossed markets to an earlier time period or eliminate a beneficial pre-opening opportunity. In this regard, Nasdaq states that it is important for market participants to use Nasdaq systems to gather information, adjust their quotations, and prepare for the market open before the market opens. Nasdaq believes that revising the Trade-or-Move requirements provides the best method for improving the quality of the market open.<sup>29</sup>

Another commenter stated that, although it generally supports Nasdaq's efforts to improve the Nasdaq opening, it believes that Nasdaq's amended proposal falls short of solving concerns surrounding the market open.<sup>30</sup> The commenter suggested that the most effective way to improve the market open is to require that the first official print in a Nasdaq stock be based upon the first unlocked and uncrossed market, thereby reflecting the true market price of the security.<sup>31</sup> In addition, the commenter stated that to provide more effective deterrence, firms that do fail to comply with Nasdaq's requirements for locked and crossed markets during the pre-opening should be taken "out of the box" and not allowed to quote for a specified period of time.<sup>32</sup> Finally, the commenter

recommended that all market participants be required to send a Trade-or-Move Message prior to locking or crossing the market.

Similarly, another commenter stated that the different Trade-or-Move Message sequence requirements for market makers and ECNs would lead to confusion.<sup>33</sup> The commenter stated that all market participants should be required to enter locking or crossing quotes either before or after sending a Trade-or-Move Message; however, the commenter preferred the former sequence.<sup>34</sup> The commenter also recommended that the Trade-or-Move requirements mandate that market participants take continuous action to resolve locked and crossed markets, either by moving the locking or crossing quote after receiving an execution or by sending another Trade-or-Move Message to trade for additional shares at the quoted price.

In response to the concerns regarding the different Trade-or-Move Message sequences for market makers and ECNs, Nasdaq states that, after carefully examining the issue, it has concluded that the proposed message sequences will reduce the instances of locked and crossed markets.<sup>35</sup> With regard to the concern that the current Trade-or-Move requirements do not require ongoing efforts to resolve locked and crossed markets, Nasdaq states that it expects to file a proposal with the Commission that will further improve the operation of the Trade-or-Move requirements and address both First Union's concern regarding the efficacy of the Trade-or-Move requirements and Morgan Stanley's suggestion that the quote requirements of a market participant that violates the Trade-or-Move requirements be removed from the market for a period of time.<sup>36</sup>

Finally, with respect to Morgan Stanley's suggestion that the first official print in a Nasdaq stock be based on the first unlocked and uncrossed market, Nasdaq states that it is considering a proposal to establish an official opening print price that accounts for Nasdaq's decentralized market structure.<sup>37</sup> Before implementing an opening print process,

Nasdaq will solicit input from its Quality of Markets Committee, its Board of Directors, and its members.<sup>38</sup>

#### **IV. Discussion**

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.<sup>39</sup> In particular, the Commission finds that the proposal, as amended, is consistent with Sections 15A(b)(6), 15(b)(11), and 11A(a)(1)(C) of the Act.<sup>40</sup> Section 15A(b)(6) of the Act requires that the rules of a national securities association be designed to promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in processing information with respect to and facilitating transactions in securities, as well as to remove impediments to and perfect the mechanism of a free and open market, and, in general, to protect investors and the public interest. Section 15(b)(11) of the Act requires that the rules of a 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. In Section 11A(a)(1)(C) of the Act, Congress found that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure: (1) Economically efficient execution of securities transactions; (2) fair competition among brokers and dealers; (3) the availability to brokers, dealers and investors of information with respect to quotations and transactions in securities; (4) the practicability of brokers executing investors orders in the best market; and (5) an opportunity for investors orders to be executed without the participation of a dealer.

Specifically, the Commission finds that Nasdaq's proposal, as amended, is designed to reduce the frequency of pre-opening locked and crossed markets, which should help to provide more informative quotation information, facilitate price discovery, and contribute to the maintenance of a fair and orderly market. The Commission believes that the proposal, as amended, addresses the concerns raised by the commenters

<sup>33</sup> See First Union Letter, *supra* note 9.

<sup>34</sup> *Id.*

<sup>35</sup> See April 15 Letter, *supra* note 11.

<sup>36</sup> See April 15 Letter, *supra* note 11. Nasdaq notes that its Quality of Market Committee and the Subcommittee considered a proposal to remove the quotations of a market participant that violated the Trade-or-Move requirements. However, Nasdaq states that it was unable to develop a solution that would effectively preserve the rights of market participants that had their quotes removed from the market involuntarily. See April 15 Letter, *supra* note 11.

<sup>37</sup> See April 15 Letter, *supra* note 11.

<sup>38</sup> See April 15 Letter, *supra* note 11.

<sup>39</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>40</sup> 15 U.S.C. 78o-3(b)(6), 15 U.S.C. 78o-3(b)(11), and 15 U.S.C. 78k-1(a)(1)(C).

<sup>24</sup> See *supra* note 7.

<sup>25</sup> See *supra* note 8.

<sup>26</sup> See *supra* note 9.

<sup>27</sup> See Levine Letter, *supra* note 9.

<sup>28</sup> See April 5 Letter, *supra* note 10.

<sup>29</sup> See April 5 Letter, *supra* note 10.

<sup>30</sup> See Morgan Stanley Letter, *supra* note 9.

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

while providing requirements designed to establish a more orderly market opening.

For example, under the revised Trade-or-Move Message sequence procedures, ECNs will send a Trade-or-Move Message prior to entering a locking or crossing quote, while market makers will send a Trade-or-Move Message after entering a locking or crossing quote. The revised procedures respond to market makers' concerns that requiring market makers to send a Trade-or-Move Message prior to entering a locking or crossing quote would necessitate substantial programming changes or require manual processing.<sup>41</sup> At the same time, the Trade-or-Move Message sequence applicable to ECNs, combined with the requirement to respond to a Trade-or-Move Message within 10 seconds, should help ECNs avoid dual liability. Specifically, the revised rule will allow an ECN to send a Trade-or-Move Message for the actual size of an agency order, wait 10 seconds for a response, and, assuming it receives no response, cancel the Trade-or-Move Message and enter the agency order as a locking or crossing quote.<sup>42</sup> The Commission also believes that the requirement to respond to a Trade-or-Move Message within 10 seconds should help to facilitate the prompt resolution of locked or crossed markets that occur.

The amended proposal will require a market participant handling a proprietary order to send a Trade-or-Move Message for a minimum of 10,000 shares in the case of Nasdaq 100 and S&P 400 issues and 5,000 shares for all other issues. The Commission believes that the 10,000-share Trade-or-Move Message size requirement may help to deter market participants entering from locking or crossing quotes in Nasdaq 100 and S&P 400 issues.

As discussed above, Nasdaq's amended proposal prohibits market participants from locking or crossing the market between 9:29:30 a.m. and 9:29:59 a.m. Market participants will, however, be permitted to send Trade-or-Move Messages for the required number of shares to any party or parties they wish to lock or cross. The recipients of such messages must respond to the message by trading in full or moving their quotes within the 10-second response time. The Commission believes that the prohibition on locking and crossing the market between 9:29:30 a.m. and 9:29:59 a.m. could help to provide for a more orderly market open,

and thereby benefit all market participants.

Finally, the three comment letters received following the publication of Amendment Nos. 2 and 3 reflect the continuing disagreement among market participants concerning the implementation of the Trade-or-Move requirements and the most effective means for providing an orderly opening on Nasdaq. In its response to the commenters, Nasdaq noted that it is developing proposals designed to address some of the concerns raised by the commenters.<sup>43</sup> The Commission expects Nasdaq to continue working to refine its procedures as necessary to achieve a more orderly market opening.

## V. Conclusion

For the foregoing reasons, the Commission finds that the proposal, as amended, is consistent with the requirements of the Act and rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>44</sup> that the proposed rule change (SR-NASD-00-76), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>45</sup>

**Margaret H. McFarland**

*Deputy Secretary*

[FR Doc. 02-13873 Filed 6-3-02; 8:45 am]

BILLING CODE 8010-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-45987; File No. SR-NYSE-2001-30]

### Self-Regulatory Organizations; The New York Stock Exchange, Inc.; Order Granting Approval of a Proposed Rule Change to Amend Rule 227 Regarding Depository Eligibility

May 28, 2002.

On August 21, 2001, the New York Stock Exchange, Inc. ("NYSE") filed with the Securities and Exchange Commission ("Commission") a proposed rule change (File No. SR-NYSE-2001-30) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of the proposed rule change was published in the **Federal Register** on April 25, 2002.<sup>2</sup> No comment letters were received. For the reasons discussed below, the

Commission is granting approval of the proposed rule change.

## I. Description

The NYSE adopted Rule 227 on June 1, 1995, for the purpose of facilitating implementation of Rule 15c6-1 of the Act that established a three-day settlement period for most securities transactions.<sup>3</sup> Rule 227, which required that domestic issuers' securities be depository eligible before they would be listed, set forth specific requirements for depository eligibility for issuers in order to facilitate the book-entry settlement of initial public offerings and to reducing the risks inherent in settling securities transactions.

On May 13, 1996, approximately one year after Rule 227 was approved, the Commission approved a rule change filed by The Depository Trust Company ("DTC")<sup>4</sup> allowing DTC to implement its Initial Public Offering ("IPO") Tracking System.<sup>5</sup> The IPO Tracking System enables lead managers and syndicate members of equity underwritings to monitor repurchases of distributed shares in an automated book-entry environment.

Currently before an issue of securities can be listed, Rule 227(a) requires each domestic issuer to represent to the NYSE that a CUSIP number identifying the security has been included in the file of eligible issuers maintained by a securities depository registered with the Commission as a clearing agency. The proposed amendments would delete the references to "domestic" and "foreign" issuers in paragraph (a). Exclusion of foreign issuers is no longer necessary because they have the capacity to comply with Rule 227 and have been doing so voluntarily for several years.

Rule 227(b) states that a security depository's inclusion of a CUSIP number in its file of eligible issues does not render a security "depository eligible" unless (1) the securities depository has an electronic system for monitoring repurchases of distributed shares at the time such shares commence trading on the Exchange or (2) when a managing underwriter elects not to deposit the securities on distribution date, it notifies the

<sup>3</sup> Securities Exchange Act Release No. 35798 (June 1, 1995), 60 FR 30909 (June 12, 1995) [File No. SR-NYSE-95-19] (order approving the adoption of NYSE Rule 227 setting forth requirements on issuers seeking to have their shares listed on the Exchange).

<sup>4</sup> DTC is a securities depository registered with the Commission under Sections 17A and 19 of the Act as a clearing agency.

<sup>5</sup> Securities Exchange Act Release No. 37208 (May 13, 1996), 61 FR 25253 (May 20, 1996) [File No. SR-DTC-95-27] (order approving implementation of DTC's IPO Tracking System).

<sup>41</sup> See, e.g., NDB Letter and Schwab Letter, *supra* note 5.

<sup>42</sup> See Amendment No. 2, *supra* note 6.

<sup>43</sup> See April 15 Letter, *supra* note 11.

<sup>44</sup> 15 U.S.C. 78s(b)(2).

<sup>45</sup> 17 CFR 200.30-3(a)(12).

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

<sup>2</sup> Securities Exchange Act Release No. 45789 (April 19, 2002), 67 FR 20568.