

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁹

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Deputy Secretary.

[FR Doc. 98-20558 Filed 7-31-98; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40262; File No. SR-NYSE-98-15]

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval to Proposed Rule Change and Amendment No. 1 to the Proposed Rule Change by the New York Stock Exchange, Inc. Seeking Permanent Approval of the Exchange's Pilot Program Concerning Entry of LOC Orders

July 24, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on May 21, 1998, the New York Stock Exchange, Inc. ("NYSE" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the NYSE. On July 16, 1998, the Exchange submitted Amendment No. 1 to the proposed rule change to the Commission.² The Commission is publishing this notice to solicit comments on the proposed rule change and Amendment No. 1 to the proposed rule change from interested persons and to grant accelerated approval to the proposed rule change, as amended.

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

The proposed rule change seeks permanent approval of the procedures for handling limit-at-the-close ("LOC") orders. The text of the proposed rule change is available at the Office of the Secretary, NYSE and at the Commission.

⁹ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² See Letter from Agnes M. Gautier, Vice President, Market Surveillance, NYSE to David Sieradzki, Attorney, Division of Market Regulation, Commission dated July 13, 1998 ("Amendment No. 1"). In Amendment No. 1, the Exchange requests accelerated approval for the proposal to allow the Exchange's procedures for limit-at-the-close orders to continue on an uninterrupted basis. As noted below, the Exchange's pilot program expires on July 31, 1998. See *infra* note 9 and accompanying text.

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 NYSE 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 III below. The NYSE 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

The proposed rule change seeks to make permanent the Exchange's pilot program for entry of LOC orders, which was first approved by the Commission on March 3, 1994.³ A LOC order is one that is entered for execution at the closing price, provided that the closing price is at or within the limit specified. NYSE Rule 13 provides, in part, that "the term 'at the close order' shall also include a limit order that is entered for execution at the closing price, on the Exchange, of the stock named in the order pursuant to such procedures as the Exchange may from time to time establish." The LOC order type has been available, on a pilot basis, for all NYSE-listed stocks since July 1995.⁴ Under the original pilot, LOC orders could be entered only to offset published imbalances of market-on-close ("MOC") order⁵ and had to be entered by 3:55 p.m. on both expiration and non-expiration days.⁶ In addition, on expiration days, LOC orders could not be canceled after 3:40 p.m., except for legitimate errors. On non-expiration days, LOC orders could not be canceled after 3:55 p.m., except for legitimate errors.⁷

³ See Securities Exchange Act Release No. 33706 (March 3, 1994), 59 FR 11093 (March 9, 1994) ("LOC Pilot Program Approval Order").

⁴ See Securities Exchange Act Release No. 35854 (June 16, 1995), 60 FR 32723 (June 23, 1995) (order approving SR-NYSE-95-09).

⁵ A MOC order is a market order to be executed in its entirety at the closing price on the Exchange. See NYSE Rule 13.

⁶ The term "expiration days" refers to both (1) the trading day, usually the third Friday of the month, when some stock index options, stock index futures and options on stock index futures expire or settle concurrently ("Expiration Fridays") and (2) the trading day on which end of calendar quarter index options expire ("QIX Expiration Days").

⁷ See LOC Pilot Program Approval Order, *supra* note 3.

In May 1997, the Exchange implemented an amended policy regarding LOC orders to permit their entry at any time during the trading day up to 3:40 p.m. on expiration days, and 3:50 p.m. on non-expiration days.⁸ Thereafter, as with MOC orders, LOC orders could not be canceled (except for legitimate errors), and could be entered only to offset published imbalances. LOC orders are subject to the same restrictions regarding order entry and cancellation as are MOC orders, as well as to the additional limitation that LOC orders yield priority to conventional limit orders at the same price.

In June 1998, the Exchange further amended its policy regarding MOC and LOC orders.⁹ Under the amended procedures, the deadline for entry of all MOC and LOC orders was set at 3:40 p.m. on all trading days. Thereafter, MOC and LOC orders cannot be canceled (except for legitimate errors), and can only be entered to offset a published imbalance. In addition, the Exchange made several changes to its rules regarding the publication of order imbalances. First, the Exchange now requires publication of all MOC/LOC imbalances of 50,000 shares or more in all stocks on any trading day as soon as practicable after 3:40 p.m. Second, the Exchange includes marketable LOC orders as well as MOC orders in the imbalance publication. Third, the Exchange is now allowing publication of MOC/LOC imbalances of any size between 3:00 p.m. and 3:40 p.m. with Floor Official approval. Finally, an additional imbalance publication will be made at 3:50 p.m. for stock that has an imbalance published at 3:40 p.m.¹⁰ These procedures are part of the current pilot for LOC orders which expires July 31, 1998.¹¹

The Commission has commented on the appropriateness of LOC orders in previous releases. For example, in its release approving the original proposal for the creation of LOC orders, the Commission noted that LOC orders could help curb excess price volatility at the close "without diminishing any benefit to investors from trading strategies which rely on MOC orders to

⁸ See Securities Exchange Act Release No. 37969 (November 20, 1996), 61 FR 60735 (November 29, 1996) (order approving SR-NYSE-96-21).

⁹ See Securities Exchange Act Release No. 40094 (June 15, 1998), 63 FR 33975 (June 22, 1998) (order approving SR-NYSE-97-36).

¹⁰ For a more complete description of the changes to the MOC/LOC program, see Securities Exchange Act Release No. 40094 (June 15, 1998), 63 FR 33975 (June 22, 1998) (order approving SR-NYSE-97-36).

¹¹ See Securities Exchange Act Release No. 38865 (July 23, 1997), 62 FR 40881 (July 30, 1998), (order approving SR-NYSE-97-19).

guarantee a fill at the closing price.”¹² In its most recent approval order for the LOC pilot, the Commission commented that since LOC orders are required to yield priority to conventional limit orders at the same price, “it is satisfied that public customer orders on the specialist book will not be disadvantaged by this proposal.”¹³ The Commission has also stated that it does not believe that allowing the use of LOC orders throughout the day would have harmful effects on other orders on the market in general.¹⁴

The Exchange has submitted three monitoring reports on LOC orders to the Commission. The reports suggest that use of LOC orders, while limited, may contribute to reducing volatility at the close. Although use of LOC orders remains limited, the Exchange believes it is appropriate to seek permanent approval for the use of LOC orders to continue to provide Exchange members with the flexibility to enter such orders, which help them to manage risk at the close.

2. Statutory Basis

The basis under the Act for the proposed rule change is the requirement under Section 6(b)(5)¹⁵ that an Exchange have rules that are designed to promote just and equitable principles of trade, to remove impediments to, and perfect the mechanism of a free and open market and, in general, to protect investors and the public interest. The proposed rule change perfects the mechanism of a free and open market by providing investors with the ability to use LOC orders as a vehicle for managing risk at the close.

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

The Exchange does not believe that the proposed rule change will 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 Member, Participants or Others

The Exchange has neither solicited nor received written comments on the proposed rule change.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing,

including whether the proposed rule change, as amended 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 at 450 Fifth Street, NW., Washington, DC 20549. Copies of such filing will also be available for inspection and copying at the principal office of the NYSE. All submissions should refer to File No. SR-NYSE-98-15 and should be submitted by August 24, 1998.

IV. Commission's Findings and Order Granting Accelerated Approval of the Proposed Rule Change

The Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b) of the Act.¹⁶ Specifically, the Commission believes the proposal is consistent with the Section 6(b)(5)¹⁷ requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts, and, in general, to protect investors and the public.¹⁸

This pilot program has been a part of the Exchange's effort to institute safeguards to minimize excess market volatility that may arise from the liquidation of stock positions related to trading strategies involving index derivative products. For instance, since 1986, the NYSE has utilized auxiliary closing procedures on expiration days. These procedures allow NYSE specialists to obtain an indication of the buying and selling interest in MOC orders at expiration and, if there is a substantial imbalance on one side of the market, to provide the investing public with timely and reliable notice thereof and with an opportunity to make

appropriate investment decisions in response.

The NYSE auxiliary closing procedures have worked relatively well and may have resulted in more orderly markets on expiration days. Nevertheless, both the Commission and the NYSE remain concerned about the potential for excess market volatility, particularly at the close on expiration days. Although, to date, the NYSE has been able to attract sufficient contra-side interest to effectuate an orderly closing, adverse market conditions could converge on an expiration day to create a situation in which member firms and their customers would be unwilling to acquire significant positions.

The Commission believes that LOC orders may provide the NYSE with an additional means of attracting contra-side interest to help alleviate MOC order imbalances both on expiration and non-expiration days. The Commission believes that LOC orders may appeal to certain market participants who might otherwise be reluctant to commit capital of the close. Specifically, unlike a MOC order, which results in significant exposure to adverse price movements, LOC orders allow each investor to determine the maximum/minimum price at which he or she is willing to buy/sell. To the extent that such risk management benefits encourage NYSE member firms and their customers to enter LOC orders to offset MOC order imbalances of 50,000 shares or more, thereby adding liquidity to the market, the Commission agrees with the NYSE that LOC orders may be a useful investment vehicle for curbing excess price volatility at the close.

The Commission also believes that the NYSE has established appropriate procedures for handling LOC orders and that the NYSE's existing surveillance should be adequate to monitor compliance with those procedures. Because LOC orders will be required to yield priority to conventional limit orders at the same price, the Commission is satisfied that public customers order on the specialist's book will not be disadvantaged by this proposal. The Commission believes that the prohibition on canceling LOC orders is consistent with the Exchange's auxiliary closing procedures and, like those procedures, should allow specialists to make a timely and reliable assessment of order flow and its potential impact on the closing price.

The Commission notes that the LOC order pilot program has been ongoing since 1994 and the NYSE has submitted detailed reports describing its experience with the pilot program. Although the use LOC orders has been

¹² See LOC Pilot Program Approval Order, *supra* note 3.

¹³ See *supra* note 9.

¹⁴ See *supra* note 8.

¹⁵ 15 U.S.C. 78f(b)(5).

¹⁶ 15 U.S.C. 78f(b).

¹⁷ 15 U.S.C. 78f(b)(5).

¹⁸ In approving this rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

limited, the use of such orders could help reduce volatility at the close. Accordingly, the Commission believes that it is reasonable and consistent with the Act for the Exchange to seek permanent approval of the LOC procedures.

The Commission finds good cause for approving the proposed rule change and Amendment No. 1 to the proposed rule change prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. Accelerated approval of the proposal will allow the NYSE to continue to use its procedures for entering LOC orders to continue on an uninterrupted basis. The Commission notes that this proposal does not make any substantive changes to the Exchange's existing LOC program. In its proposal, the Exchange simply requests permanent approval of its existing LOC program. Further, the Commission notes that the last substantive change to the LOC program was published for the full notice and comment period and the Commission received no comments on that proposal.¹⁹ Accordingly, the Commission does not believe that the current filing raises any new regulatory issues. Therefore, the Commission believes it is consistent with Section 6(b)(5) and Section 19(b)(2) of the Act to grant accelerated approval to the proposed rule change.²⁰

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,²¹ that the proposed rule change (SR-NYSE-98-15) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²²

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 98-20557 Filed 7-31-98; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40266; File No. SR-NYSE-98-16]

Self-Regulatory Organizations; Notice of Filing and Order Granting Partial Accelerated Approval of a Proposed Rule Change and Amendment No. 1 to the Proposed Rule Change by the New York Stock Exchange, Inc., Relating to Margin Requirements for Exempted Borrowers and Good Faith Accounts

July 27, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 30, 1998, the New York Stock Exchange, Inc. ("NYSE" or "Exchange") filed with the Securities Exchange Commission ("SEC" or "Commission") a proposed rule change to amend NYSE Rule 431, "Margin Requirements," to accommodate certain recent changes to the federal margin requirements. The proposal, which is described in Items I, II, and III below, which Items have been prepared by the NYSE, originally was approved by the Commission on a temporary basis until July 27, 1998.³ On July 24, 1998, the NYSE amended its proposal to request that the Commission approve the NYSE's proposal for six months on an accelerated basis.⁴ The Commission is publishing this notice and order to solicit comments from interested persons on the proposed rule change and to grant accelerated approval to the portion of the proposal that requests an extension of the proposal for six months, until January 27, 1999, or until the Commission approves the proposal permanently, whichever occurs first.⁵

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 39813 (March 27, 1998), 63 FR 16849 (April 6, 1998) (order approving File No. SR-NYSE-98-08) ("March Approval Order").

⁴ See Letter from James E. Buck, Senior Vice President and Secretary, NYSE, to Richard C. Strasser, Assistant Director, Division of Market Regulation, Commission, dated July 23, 1998 ("Amendment No. 1"). In addition, Amendment No. 1 modifies the proposal to: (1) clarify that the proposal amends the definition of "customer" in NYSE Rule 431(a)(2) to codify the Exchange's position that exempted borrowers will remain exempt from the provisions of NYSE Rule 431; and (2) correct a reference in NYSE Rule 431(a)(2) to the Board of Governors of the Federal Reserve System ("FRB").

⁵ The NYSE confirmed that the Exchange is seeking to extend the changes to NYSE Rule 431 that were approved in the March Approval Order for six months or until the Commission approves the changes on a permanent basis, whichever occurs first. Telephone conversation between Mary Anne Furlong, Attorney, NYSE, and Yvonne

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

On March 27, 1998, the Commission approved until July 27, 1998, an NYSE proposal to apply the maintenance margin requirements of NYSE Rule 431 to good faith accounts and to provide that the proprietary accounts of introducing broker-dealers that are "exempted borrowers" as that term is defined in Regulation T⁶ will continue to be subject to NYSE Rule 431(e)(6) as applicable.⁷ The NYSE requests permanent approval of the changes to NYSE Rule 431 that were approved on a temporary basis in the March Approval Order. In addition, the NYSE requests that the Commission extend the changes to NYSE Rule 431 that were approved in the March Approval Order for six months, until January 27, 1999, or until the Commission approves the changes to NYSE Rule 431 on a permanent basis, whichever occurs first.⁸

Copies of the proposed rule change are available at the NYSE and at the Commission

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 NYSE included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposal. The text of these statements may be examined at the places specified in Item V below. The NYSE has prepared summaries, set forth in Section 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

In January 1998 the FRB amended Regulation T, which governs initial extensions of credit to customers and broker-dealers.⁹ Among other things, these amendments established a "good faith" account, which can be used for transactions in non-equity securities.¹⁰

Fratlicelli, Attorney, Division of Market Regulation, Commission, on July 27, 1998 ("July 27 Conversation").

⁶ 12 CFR 220. Regulation T, "Credit by Brokers and Dealers," is administered by the FRB pursuant to section 7 of the Act.

⁷ See March Approval Order, *supra* note 3.

⁸ See Amendment No. 1, *supra* note 4, and July 27 Conversation, *supra* note 5.

⁹ See Docket Nos. R-905, R-0923, and R-0944, 63 FR 2806 (January 16, 1998).

¹⁰ 12 CFR 220.6.

¹⁹ See Securities Exchange Act Release No. 40094 (June 15, 1998), 63 FR 33975 (June 22, 1998) (order approving SR-NYSE-97-36).

²⁰ 15 U.S.C. 78f(b)(5) and 78s(b)(2).

²¹ 15 U.S.C. 78s(b)(2).

²² 17 CFR 200.30-3(a)(12).