

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40961; File No. 10-100]

Exempted Exchanges; AZX, Inc.; Amendment to Application for Exemption From Registration as an Exchange Under Section 5 of the Securities Exchange Act of 1934; Request for Comments

January 22, 1999.

I. Introduction and Summary

AZX, Inc. operates the Arizona Stock Exchange ("AZX"), a computerized, single-price auction system that facilitates trading of registered equity securities by broker-dealers and institutions. AZX operates three off-hours auctions in Nasdaq National Market ("NNM") and exchange listed securities, at 9:15 a.m., 4:20 p.m., and 5:00 p.m. (ET), each trading day. AZX also operates one auction during regular trading hours,¹ at 10:30 a.m. (ET), for NNM securities only. AZX operates pursuant to the terms and conditions of a Commission order granting AZX a "limited volume" exemption from registration as a national securities exchange² and a staff no-action letter with respect to the nonregistration of AZX as a broker-dealer, clearing agency, transfer agent, and exclusive securities information processor.³ Under the terms of its exemption, AZX trades only NNM securities during regular trading hours.⁴ Although the statute provides no guidelines as to what level of volume qualifies as "limited," the Exemption Order stated that the Commission may rescind the exemption and require AZX to register as a national securities exchange if AZX's volume exceeds that of any of the registered stock exchanges.

On July 30, 1998, AZX, Inc. filed with the Commission pursuant to Rule 6a-1 under the Securities Exchange Act of

1934 ("Act"),⁵ an amendment to its application for exemption from registration as a national securities exchange. In its amendment, AZX proposes to operate two additional auctions during regular trading hours, at 12:30 p.m. and 2:30 p.m. (ET) each trading day. AZX also proposes to trade exchange-listed and NNM securities during all three regular hours auctions. In addition, AZX proposes to consolidate its two evening after-hours auctions into one after-hours auction ending at 4:30 p.m. (ET).

If the proposal is approved, there will be five AZX auction—two off-hours and three regular hours. All five auctions will be permitted to trade both exchange-listed and NNM securities, and will be subject to real-time transaction reporting under the National Association of Securities Dealers, Inc. ("NASD") rules.⁶

The Commission is soliciting public comment on whether it is appropriate to amend the Exemption Order to reflect AZX's proposal to add two auction sessions during regular trading hours for exchange-listed and NNM securities, trade exchange-listed securities at all day auctions, and consolidate AZX's two off-hours evening auctions.⁷

II. Additional Trading Sessions

The proposed regular trading hours auctions are to be operated in the same manner as the morning auction held during regular trading hours. However, the proposal would allow exchange-listed securities, as well as NNM securities, to be traded during all three regular trading hours auctions. Commenters are invited to express their views on whether trading listed securities during regular trading hours is consistent with the language of Section 5 of the Act⁸ governing limited volume exemptions or whether it will affect AZX's ability to comply with the terms and conditions of its Exemption Order.⁹ Commenters may also wish to

express their views on whether (1) the Commission should impose additional conditions on AZX in light of the proposed changes, (2) the proposal affects AZX participants' obligations under the order handling rules,¹⁰ or (3) the proposal raises issues regarding surveillance by AZX of trading activity in listed securities. In this regard, in connection with its current regular hours auction for NNM Securities, AZX undertook to implement surveillance procedures to detect possible market manipulation and insider trading. These procedures require AZX to compare auction prices and bids and offers entered into AZX with activity in the primary market, and to monitor the effects of an order cancellation or revision on the primary market. Commenters may wish to comment on whether these surveillance procedures are sufficient for monitoring both NNM and exchange-listed securities.

III. Solicitation of Comments

The Commission is soliciting public comment on whether to amend the AZX Exemption Order to reflect the trading sessions during regular trading hours for exchange listed and NNM securities, the trading of exchange listed securities at its 10:30 (ET) auction, and the consolidation of its two after hours evening auctions. 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. All comment letters should refer to File No. 10-100. Copies will be available for inspection and copying in the Commission's Public Reference Room in Washington, DC. All submissions should refer to the file number in the caption above and should be submitted by March 3, 1999.

(3) the submission of activity reports to the Commission; (4) the adoption and implementation of procedures to conduct surveillance of trading by AZX employees and to detect possible insider trading or manipulative abuses; (5) continued compliance with the capacity, security and contingency plan requirements of the Commission's Automation Review Policy; and (6) the provision of 30 days prior notice of any material changes in the operation of the auction.

¹⁰The Division of Market Regulation ("Division") previously issued a letter confirming that AZX is not an electronic communications network ("ECN") as defined in Rule 11Ac1-1 under the Act (17 CFR 240.11Ac1-1). Letter from Richard R. Lindsey, Director, Division, SEC, to R. Steven Wunsch, President, AZX, Inc., dated January 14, 1997. Because AZX is not an ECN, market maker participants entering priced orders into AZX will not be required to update their market maker quotes to reflect their AZX orders under the amendments to the Quote Rule.

¹ "Regular trading hours" refers to the time period in which the New York Stock Exchange, Inc. permits trading, which is 9:30 a.m. to 4:00 p.m. (ET) each trading day.

² Securities Exchange Act Release No. 28899 (February 20, 1991), 56 FR 8377 (February 28, 1991), amended by Securities Exchange Act Release No. 37272 (June 3, 1996), 61 FR 29145 (June 7, 1996) (collectively "Exemption Order").

³ Letter regarding Wunsch Auction Systems, Inc., predecessor to AZX, Inc., (February 28, 1991). The no-action letter also provided AZX's original crossing broker, Bankers Trust Brokerage Corporation ("BTBC") with relief with respect to non-registration as an exchange, clearing agency, transfer agent, and exclusive securities information processor. BTBC was replaced as AZX's crossing broker by Investment Technology Group, Inc. ("ITG") in February 1995. ITG is a registered broker-dealer.

⁴ See Securities Exchange Act Release No. 37272, *supra* note 2.

⁵ 17 CFR 240.6a-1

⁶ See NASD Rules 4630, 4631, 4632, 6400, 6410 and 6420.

⁷ Notwithstanding a statement to the contrary contained in the application, the Commission has not previously approved any portion of AZX's proposal.

⁸ 15 U.S.C. 78(e).

⁹ The most significant terms and conditions include: (1) the continued registration of AZX's crossing-broker as a broker-dealer under Section 15(b) of the Act and the continued membership of AZX's crossing-broker in at least one self-regulatory organization; (2) the effective registration of any security traded on AZX under Sections 12(b) or 12(g) of the Act, or the provision of information with respect to a security pursuant to Section 15(d) of the Act, or an exemption from registration because the security is a "government security" as defined in Section 3(a)(42)(A), (B), or (C) of the Act;

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Rel. No. IC-23662; 812-10916]

The Victory Portfolios, et al.; Notice of Application

January 25, 1999.

AGENCY: Securities and Exchange Commission ("SEC").

ACTION: Notice of application for an order under section 17(d) of the Investment Company Act of 1940 (the "Act") and rule 17d-1 under the Act.

SUMMARY OF APPLICATION: Applicants request an order to permit The Victory Portfolios to deposit uninvested cash balances in joint accounts investing in short-term investments, and to permit Key Trust Company of Ohio, N.A. ("Key Trust") to accept fees for acting as securities lending agent.

Applicants: The Victory Portfolios (consisting of Victory Balanced Fund, Victory Convertible Securities Fund, Victory Diversified Stock Fund, Victory Established Value Fund, Victory Federal Money Market Fund, Victory Financial Reserves Fund, Victory Fund for Income, Victory Government Mortgage Fund, Victory Gradison Government Reserves Fund, Victory Growth Fund, Victory Institutional Money Market Fund, Victory Intermediate Income Fund, Victory International Growth Fund, Victory Investment Quality Bond Fund, Victory Lakefront Fund, Victory LifeChoice Conservative Investor Fund, Victory LifeChoice Growth Investor Fund, Victory LifeChoice Moderate Investor Fund, Victory Limited Term Income Fund, Victory National Municipal Bond Fund, Victory New York Tax-Free Fund, Victory Ohio Municipal Bond Fund, Victory Ohio Municipal Money Market Fund, Victory Ohio Regional Stock Fund, Victory Prime Obligations Fund, Victory Real Estate Investment Fund, Victory Special Growth Fund, Victory Special Value Fund, Victory Stock Index Fund, Victory Tax-Free Money Market Fund, Victory U.S. Government Obligations Fund, Victory Value Fund (each a "Fund")), Key Asset Management Inc. ("KAM"), and Key Trust.¹

¹ Applicants request that the relief apply to all existing and future series of The Victory Portfolios and any other registered management investment companies for which KAM or any entity

Filing Dates: The application was filed on December 22, 1997, and amended on October 5, 1998, and on December 14, 1998.

Hearing or Notification of Hearing: An order granting the application will be issued unless the SEC orders a hearing. Interested persons may request a hearing by writing to the SEC's Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the SEC by 5:30 p.m. on February 18, 1999, and should be accompanied by proof of service on applicants, in the form of an affidavit or, for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the SEC's Secretary.

ADDRESSES: Secretary, SEC, 450 Fifth Street, NW, Washington, DC 20549. Applicants, 3435 Stelzer Road, Columbus, OH 43219.

FOR FURTHER INFORMATION CONTACT: Lisa McCrea, Attorney Adviser, at (202) 942-0562, or Mary Kay Frech, Branch Chief, at (202) 942-0564 (Office of Investment Company Regulation, Division of Investment Management).

SUPPLEMENTARY INFORMATION: The following is a summary of the application. The complete application may be obtained for a fee at the SEC's Public Reference Branch, 450 5th Street NW, Washington, DC 20549 (tel. 202-942-8090).

Applicant's Representations

1. The Victory Portfolios is an open-end management investment company registered under the Act, currently consisting of thirty-two Funds. KAM is registered as an investment adviser under the Investment Advisers Act of 1940, and serves as investment adviser to the Funds. Both KAM and Key Trust are subsidiaries of KeyCorp.

2. All of the Funds are authorized by their investment policies to invest in short-term liquid assets including repurchase agreements, United States government securities, or other short-term debt obligations. The investment objectives, policies and restrictions of most Funds permit them to engage in securities lending transactions. No Fund

controlling, controlled by, or under common control with KAM acts as investment adviser. Each existing registered management investment company that currently intends to rely on the requested order has been named as an applicant. Any other existing or future registered investment companies that subsequently rely on the order will comply with the terms and conditions in the application.

will engage in securities lending unless so permitted.

3. Applicants propose to deposit uninvested cash balances of participating Funds ("Participants") that remain at the end of the trading day and/or cash for investment purposes ("Uninvested Cash") into one or more joint accounts (the "Joint Investment Account"). Applicants also propose to deposit the cash received as collateral in a securities lending transaction ("Cash Collateral") in a joint account ("Joint Collateral Account", together with the Joint Investment Account, the "Joint Accounts").

4. The Joint Accounts will be established at Key Trust, the Funds' custodian, and the daily balance of the Joint Accounts will be invested in the following short-term investments: (a) Repurchase agreements that are collateralized fully within the meaning of rule 2a-7 under the Act;² (b) interest-bearing or discounted commercial paper, including dollar denominated commercial paper of foreign issuers; and (c) any other short-term taxable and tax-exempt money market instruments, including variable rate demand notes, that constitute "Eligible Securities" within the meaning of rule 2a-7 under the Act (collectively, "Short-Term Investments").

5. Applicants also propose to permit Key Trust to act as the Funds' securities lending agent, to invest the Cash Collateral at the direction of KAM in Short-Term Investments, and to enter into a fee splitting arrangement with the Funds whereby Key Trust would receive a fee based on a percentage of the net returns generated by the lending transactions. Under the proposed arrangement, Key Trust would receive a pre-negotiated percentage of the net earnings on the investment of the Cash Collateral.

6. A Participant's decision to use a Joint Account would be based on the same factors as its decision to make any other Short-Term Investment. Key Trust, at the direction of KAM, would be responsible for investing funds held by the Joint Accounts, establishing accounting and control procedures, operating the Joint Accounts in accordance with the procedures discussed below, and ensuring fair treatment of Participants. KAM (or Key Trust at KAM's direction) would manage investments in the Joint Accounts in essentially the same manner as if it had invested in the instruments on an individual basis for each Participant. All purchases through

² Applicants will not invest in hold-in-custody repurchase agreements.