utilized with respect to any conventional equity options position, not just that portion of the position that was established pursuant to the NASD's Equity Option Hedge Exemption, will enable market participants to establish larger positions in conventional equity options and, thus, will help to ensure that participants in the OTC options market are not placed at a competitive disadvantage vis-a-vis the exchange markets. In addition, NASD Regulation believes that increasing the position limits for conventional equity options will afford market participants, particularly portfolio managers, issuers, and sophisticated institutional investors, greater flexibility to employ larger options positions when effectuating their investment strategies.

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

The Association does not believe that the proposed rule change will impose any inappropriate burden on competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were either solicited or received.

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

Within 35 days of the 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 the 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, 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 at the Commission's Public Reference Room, located at the above address. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR–NASD–98–23 and should be submitted by May 19, 1998.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[13]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 98–11169 Filed 4–27–98; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39892; File No. SR–NASD–98–18]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Qualified Immunity in Arbitration Proceedings for Statements Made on Forms U–4 and U–5

April 21, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] notice is hereby given that on April 21, 1998, NASD Regulation, Inc. (''NASD Regulation'') 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 NASD Regulation. 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

NASD Regulation is proposing to add a new rule to the Rules of the National Association of Securities Dealers, Inc. (''NASD'' or ''Association''), to provide members of the NASD with qualified immunity in arbitration proceedings for statements made in good faith in certain disclosures filed with the NASD on Forms U–4 and U–5, the uniform registration and termination notices for registered persons. Below is the text of the proposed rule change.

Proposed new language is in italics.

* * * * *

Rule 1150. Regulatory Form Disclosures

(a) Mandatory Disclosures

A member must make truthful and accurate statements on the covered forms required under Article V, Sections 2 and 3 of the By-Laws.

(b) Qualified Immunity

(1) This paragraph shall apply to any arbitration proceeding between a member or other party and a covered person relating to statements made in response to an information requirement of a covered form with respect to such covered person, to the extent that such statements are contained in a covered form that has been or, at a subsequent point in time, is (A) filed with a regulatory authority or self-regulatory organization, and (B) disseminated by reason of such filing, or otherwise disseminated orally, in writing, or through any electronic medium to an appropriate person.

(2) A defending party shall not be liable in a proceeding to a covered person for any defamation claim related to an alleged untrue statement that is contained in a covered form if the statement was true at the time that the statement was made.

(3) A defending party shall not be liable in a proceeding to a covered person for any defamation claim related to an alleged untrue statement that is contained in a covered form unless the covered person shows by clear and convincing evidence that:

(A) the defending party knew at the time that the statement was made that it was false in any material respect; or

(B) the defending party acted in reckless disregard as to the statement's truth or falsity.

(c) Definitions

For purposes of this Rule:

(1) The term ''appropriate person'' means any federal or state governmental or regulatory authority, and self-regulatory organization, any employer or prospective employer of a covered person, or any person who requests or is required to obtain information concerning the covered person from the defending party and as to whom the defending party has a legal obligation to provide such information.

(2) The term ''claim'' means any claim, counterclaim, third-party claim, or cross-claim.

(3) The term ''covered form'' means any form or notice required under

[13] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. § 78s(b)(1).

Article V, Sections 2 and 3 of the By-Laws, including Forms U–4 and U–5. Disclosure Reporting Pages, and related explanatory materials.

(4) The term ''covered person'' means any present or former registered person or other employee of a member who is a party to a proceeding relating to a dispute within the scope of this Rule.

(5) The term ''defending party'' means any member who is a party to a proceeding and who is adverse to a covered person who is a party, and any associated person of such member.

(Rule 1150 is effective beginning on (Date) 1998 and ending on (Date) 2002, and applies to claims relating to any covered forms, as defined in Rule 1150, that are filed during that period.)

* * * * *

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

In its filing with Commission, NASD Regulation included statements concerning the purpose of, and statutory 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. NASD Regulation 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

Summary. The proposed rule is designed to deal with the prospect that member firms may be reluctant to make complete disclosures on forms required to be filed with the NASD because of the potential for lawsuits relating to defamation claims by former or present employees. The proposed rule would create a uniform qualified immunity standard for statements made in good faith in certain disclosures filed with the NASD on Forms U–4 and U–5. To overcome this qualified immunity, a registered person would have to prove in an arbitration proceeding by clear and convincing evidence that the member firm knew at the time the statement was made that it was false in any material respect, or that the member acted in reckless disregard to the statement's truth or falsity. For purposes of NASD arbitration, the rule would supersede state law on the same subject.

Background. This issue arises primarily in the context of filings made on Form U–5 following termination of employment of a registered person. The NASD By-Laws (Article V, Section 3) require that the member give notice of the termination to the NASD within 30 days after the termination, and that the member provide a copy simultaneously to the registered person. The By-Laws also require that the member notify the NASD, and send a copy to the registered person, within 30 days if the member learns of facts or circumstances causing any information in the prior notice to become inaccurate or incomplete.

Form U–5, which is entitled the ''Uniform Termination Notice for Securities Industry Registration,'' is a form used throughout the securities industry at both the federal and state level. It requires that the member indicate the reason for the termination by checking one of the blocks labeled Voluntary, Deceased, Permitted to Resign, Discharged, or Other. If one of the last three blocks is checked, the member must provide an explanation. Regardless of the block checked, the member also must indicate whether the registered person, during the period of his or her association with the member, was involved in certain types of disciplinary actions, the subject of a customer complaint, convicted of certain crimes, or under investigation or internal review.

In recent years, registered persons have brought, primarily in arbitration, a number of defamation [2] claims for allegedly untrue or misleading statements made on the Form U–5.[3] Because of the financial interests at issue the potential for substantial damages may exist in a number of cases. The NASD believes that the potential for liability, or for inconsistent standards of liability, is a significant disincentive for firms to provide full and fair disclosure. Failure to make full disclosure of disciplinary problems has the potential to compromise the integrity of the Central Registration Depository, and hinders enforcement action by the NASD and other regulators. At the same time, the NASD believes it is important that any solution provide adequate protection to employees from statements designed to penalize unfairly a departing employee, or to prevent him or her from obtaining new employment or attracting existing customers to another member firm where the person has subsequently become employed.

Development of the Rule Proposal. The NASD met periodically during 1997 to discuss defamation issues with representatives of member firms, the Securities Industry Association, the New York Stock Exchange (''NYSE''), the North American Securities Administrators Association, and attorneys who often represent registered representatives in court litigation and in arbitration proceedings.

Many members of the industry favored a regulatory standard providing for absolute immunity. Most state court decisions that have considered this issue in the Form U–5 or in similar contexts have adopted a qualified immunity standard. However, one New York state court decision has expressly recognized an absolute immunity standard with respect to statements contained in the Form U–5.[4] Those states that, by court decision or statute, have adopted a qualified immunity standard in the same or similar contexts, require that falsity or recklessness be proved either by ''preponderance of the evidence'' or by ''clear and convincing evidence,'' as discussed below.

In order to obtain as many views as possible, the NASD published a draft of the proposed rule change in a Notice to Members (''NTM 97–77'') that was mailed to member firms and other subscribers, and was also posted on the NASD Regulation Web site and sent to a group of attorneys who represent employees, to registered representatives

[2] ''Defamation'' has been defined as an ''intentional false communication, either published or publicly spoken, that injures another's reputation or good name.'' *Black's Law Dictionary* 417 (6th ed. 1990). ''Libel'' (written defamation) and ''slander'' (spoken defamation) are both methods of defamation. *Id* at 1388.

[3] Defamation claims may also arise with respect to disclosures on Form U–4, which is required to be filed by registered persons upon the occurrence of certain events, but which in practice is often drafted by the member firm with which the individual is associated.

[4] *Herzfeld & Stern, Inc.* v. *Beck*, 572 N.Y.S.2d 683 (N.Y. App. Div. 1991), *appeal dismissed*, 79 N.Y.2d 917 (1992). The court reasoned that federal law had established a comprehensive system of oversight and self-regulation by the NYSE in order to ensure adherence by members of the industry to both the statutory mandates and ethical standards of the profession, and concluded that the NYSE's disciplinary function conforms to the requirements of a quasi-judicial administrative proceeding. Therefore, statements made on a Form U–5 and later used as the basis for an NYSE investigation were considered ''statements uttered in the course of a judicial or quasi-judicial proceeding [which are] absolutely privileged so long as they are material and pertinent to the questions involved notwithstanding the motive with which they are made.'' *Id.* at 683. *But see Fleet Enterprises, Inc.* v. *Velinsky*, No. 604462/96 (N.Y. Sup. Ct. Jan. 16. 1997), in which a lower court in New York rejected a brokerage firm's petition, on absolute privilege grounds, to stay the arbitration of Form U–5 defamation claims, and ordered arbitration to proceed, applying the Federal Arbitration Act as to the issue of arbitrability. The court stated that ''whether New York substantive law will apply to Velinsky's claims in arbitration is for the arbitrator to decide.'' Slip op. at 5. *See also Fahnestock & Co., Inc.* v. *Waltman*, 935 F.2d 512 (2d Cir. 1991); *Culver* v. *Merrill Lynch & Co., Inc.*, 1995 U.S. Dist. Lexis 10017 (S.D.N.Y. 1995).

groups, and to others. That proposal included a provision that would require member firms to give notice of the contents of a Form U–5 (and amendments) to the subject of the form at least ten days prior to filing the form, and would require members to provide immediate notification to employees of material revisions to be filed on Form U–5. Fifty-three comments were received and considered by the NASD. The advance notice provision was the subject of almost universal criticism, as described below. A revised proposal was approved by the NASD Regulation and NASD Boards in January 1998.

Details of the Proposed Rule. The proposal rule would provide that members and associated persons will not be liable to an employee for a claim that is related to an alleged untrue statement contained in Form U–4 or U–5 pertaining to the employee, unless the employee can prove by clear and convincing evidence that the defending party knew that the statement was false in any material respect, or acted in reckless disregard as to its truth or falsity.

As noted above, state law standards generally provide for some type of qualified immunity for statements of the type that are required by the covered forms, and therefore the rule may not represent a substantial change in the standard that would apply in a given case, but will instead provide a uniform standard to which parties and arbitrators can look for guidance. NASD Regulation in concerned, however, that the proposal not signal a willingness to tolerant false or malicious statements by member firms with respect to their employees, either through disclosures on the covered forms or through other venues. Any such statements clearly violate the obligation of members to provide accurate information to NASD Regulation and are inconsistent with just and equitable principles of trade.

In particular, NASD Regulation is concerned with the potential that disclosures contained on covered forms may be used deliberately by one member to limit the mobility of registered persons who have determined to find employment with another member, or to delay the effectiveness of the transfer of employment.[5] As noted, such conduct would be grounds for disciplinary action, and during the rule's pilot period, NASD Regulation intends to consider and investigate evidence of misuse of covered forms other forms, or regulatory processes for improper purpose. In addition, NASD Regulation will provide a mechanism through its Internet Web Site to obtain input from employees, member firms, and others as to the operation of the pilot program and to report potential abuses. To the extent that NASD Regulation determines that misuse of regulatory processes has increased during the pilot period, it may determine to modify or terminate the rule prior to the end of that period. Finally, NASD Regulation will provide training to arbitrators to ensure that they are cognizant of these concerns, that they understand the application of the rule, and that the rule is applied only with respect to appropriate types of claims.[6]

Paragraph (a) of the proposed rule states that members must provide truthful and accurate statements in response to the information requirements of the forms required under Sections 2 and 3 of Article V of the Association's By-Laws, *i.e.*, Forms U–4 and U–5 and attachments to those forms. This paragraph make clear that the purpose of the proposed rule is to further the goal of accurate disclosure, and is intended to reaffirm the existing disclosure obligation of NASD members as set forth in the By-Laws. The word ''complete'' was deleted from the draft version of the proposed rule, to address the concern of some commenters that this language could be construed as adding a new but vague requirement of ''completeness'' and could create liability beyond that contemplated by the By-Laws.

The proposed rule would apply to statements made on ''covered forms.'' Covered forms are defined in paragraph (c)(3) to include forms or notices required under Article V, Sections 2 and 3 of the By-Laws, including Disclosure Reporting Pages and other explanatory materials attached to the forms or notices. Although the area of greatest focus has involved the filing of Form U–5 in connection with employee terminations, members of the industry have indicated that required disclosures pertaining to employees on Form U–4 provide the same potential for liability, and NASD Regulation believes that the same regulatory interests in complete disclosure apply to statements on that form. The rule would apply to statements made by a member firm on a covered form with respect to a present or former employee of the firm. The rule would also apply to the liability of both member firms and associated persons, and accordingly would apply to both the signatory of the form or other persons involved in the preparation of the form as well as the member itself.

The rule as proposed in NTM 97–77 would have required members to provide employees with copies of proposed language on Form U–5 describing the reason for termination at least ten days before the filing of the form or an amendment to the form. In addition, members would have been required to provide to the employee immediate notice of revisions to the proposed language. The purpose of these provisions was to provide employees with an opportunity to seek amended disclosure language when they could demonstrate obvious inaccuracies.

After further review, NASD Regulation has determined to delete these provisions in light of the comments received. The comments of both members and registered representatives were overwhelmingly negative with regard to this part of the proposal. Many commenters expressed the view that these provisions would lead to ''negotiated'' or ''watered down'' disclosure, and some suggested that it could compromise ongoing internal investigations. Some commenters stated that the period was too short for meaningful review of the Form U–5, while other commenters felt that the period was too long in that it left broker/dealers only 20 days within which to prepare the forms and mail them to employees, since Form U–5 must be filed with the NASD within 30 days after termination. Some commenters pointed out that employees already have an opportunity to comment on certain reportable events through filing of an amended Form U–4.

The proposed rule would provide qualified protection to statements only to the extent that they are contained in a covered form that has been or, at a subsequent point in time, is filed with any federal or state regulatory authority, or self-regulatory organization, and are disseminated to ''appropriate persons.'' Therefore, oral statements are covered by the qualified immunity only to the extent that they track language that is already or later incorporated into the covered form. In this context, paragraph (c)(1) of the proposed rule defines ''appropriate persons'' to include, in addition to regulatory organizations, current or prospective employers and others who affirmatively request information concerning the employee

[5] NASD Rule 10335 of the Code of Arbitration Procedure contains special provisions for injunctive relief in circumstances where fast interim relief is necessary.

[6] Because the rule as proposed would apply only to claims for defamation, it would not affect other claims, *e.g.*, tortuous interference with contractual relations, to the extent that such claims would constitute substantially different causes of action and not merely recharacterization of defamation claims.

and as to whom the member has an obligation to provide the information. The latter provision is designed to ensure that the rule would apply to requests from persons as to whom applicable legal standards require the disclosure of the information.

Paragraph (b)(2) of the proposed rule provides that a defending party shall not be liable for a defamation claim if the statement was true at the time that the statement was made. As noted above, Article V, Section 3 of the NASD By-Laws already requires that the member notify the NASD, and send a copy to the registered person, within 30 days if the member learns of facts or circumstances causing any information in the prior notice to become inaccurate or incomplete.

Paragraph (b)(3) of the proposed rule contains the basic legal standard found in federal and state court decisions that recognize a qualified immunity in various contexts. The courts do not, however, consistently define the burden of proof that a plaintiff must meet in order to show that a false statement was made knowingly or recklessly. Some decisions apply the ''preponderance of the evidence'' standard that most commonly applies to claims and defenses in civil litigation. Others apply a stricter ''clear and convincing'' standard. In some cases, decisions in the same jurisdiction conflict on this point. The NASD believes that, because no one standard is dominant, the standard applied should be the one that will reach best the goals to which the proposed rule is addressed. The NASD has determined that the ''clear and convincing'' standard provides a good balance, in that it provides some protection to member firms against defamation claims for statements they are required to provide, while still providing that members are liable for clear cases of abusive or malicious disclosure.

NTM 97–77 asked for comment as to whether NASD Regulation should seek to provide a mandatory pre-filing or arbitration procedure to resolve termination disputes prior to the 30-day period following termination in which the Form U–5 is required to be filed. Most of the comments addressing this issue suggested that such a procedure could not effectively resolve disputes within this time frame. NASD Regulation has determined that a mandatory procedure would raise too many difficult practical and timing issues to be useful, but will endeavor to provide mediators on an expedited basis when both parties are interested in resolving disputes at an early stage.

The proposed rule would apply for a pilot period of four years. Prior to the end of that period, the staff will review a sample of filings made during the period of the rule's effectiveness to attempt to gauge the nature and quality of disclosure that has been provided, in contract with forms filed prior to the pilot period.

2. Statutory Basis

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that the Association's rule must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The NASD believes that the proposed rule change will encourage fuller disclosure by member firms of any regulatory problems concerning a registered representative and thus provide more complete information to the investing public through the Public Disclosure Program and to other broker/dealers through the Central Registration Depository.

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

NASD Regulation 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

The proposed rule change was published for comment in NASD Notice to Member 97–77 (November 1977). Fifty-three comments were received in response to the Notice.

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 for foregoing, 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 NASD. All submissions should refer to file number SR–NASD–98–18 and should be submitted by May 19, 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. 34–39903; File No. SR–NYSE–98–13]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc. Relating to the Trading of Bonds

April 22, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] notice is hereby given that on April 15, 1998, 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 NYSE. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

[7] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).