record to a registered clearing agency, obtain a control number, cross reference the control number to the confirmation/acknowledgment, electronically deliver any acknowledgment received from a customer or a customer's agent to the registered clearing agency and include such control number when delivering acknowledgments to the clearing agency.

- Certify to the integrity and capacity of the electronic confirmation/acknowledgment system and that it will maintain monitoring and contingency procedures.
- On an annual basis, submit an independent auditor's report to the Commission staff which the Commission staff does not object to.
- Notify the Commission staff in writing of any material changes in the systems by which it offers electronic confirmation/acknowledgment services.
- Submit to the Board copies of any of the above filings with the Commission staff within ten business days.
- Supply supplemental information regarding its confirmation/acknowledgment services, as requested by the Board or the Commission staff.

The Board believes that these requirements for a vendor to become and remain qualified are necessary to assure that the confirmation/acknowledgment services used in the securities industry are reliable and are integrated into the national system of clearance and settlement. The proposed rule change is responsive to the Commission staff's request (contained in a letter, dated November 25, 1997 from Mr. Richard R. Lindsey, Director, Division of Market Regulation) that SROs consider adoption of uniform rule amendments which allow vendors to provide confirmation/acknowledgment services under circumstances similar to those specified in the proposed rule change.[5]

(b) As set forth in Section 15B(b)(2)(C) of the Act,[6] the Board has the authority to adopt rules to ''foster cooperation and coordination with persons engaged in . . . clearing, settling, processing information with respect to, and facilitating transactions in municipal securities.''

The Board's role in this area is given additional direction by Section 17A of the Act,[7] which mandates the creation of a national system of automated clearance and settlement of securities transactions. Section 17A expressly includes municipal securities within the stated objectives.

(B) Self-Regulatory Organization's Statement on Burden on Competition

The Board does not believe that the proposed rule change will have any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act because it applies equally to all brokers, dealers and municipal securities dealers involved in DVP/RVP customer transactions.

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

No written comments were solicited or received.

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

Within thirty-five 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 ninety 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 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 in the Commission's Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing also will be available for inspection and copying at the principal office of the Board. All submissions should refer to File No. SR–MSRB–98–06 and should be submitted by May 4, 1998.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.[8]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 98–9593 Filed 4–10–98; 8:45 am]

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[5] The Commission notes that the proposed rule change addresses the concerns raised by the Petition for Rulemaking filed by Thomson Financial Services (''Thomson'') with the Commission in December 1996. Thus, the Commission will respond to Thomson's petition after the final disposition of the proposed rule change.

[6] 15 U.S.C. 78o–4(b)(2)(C).

[7] 15 U.S.C. 78q–1.

[8] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39831; File No. SR–NASD–98–20]

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing of Proposed Rule Change Relating to Permitting Qualified Vendors to Provide Confirmation and Affirmation Services to Institutional Customers

April 6, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] notice is hereby given that on March 5, 1998, the National Association of Securities Dealers, Inc. (''NASD'' or ''Association'') 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 primarily by the NASD. The Commission is publishing this notice to solicit comments from interested persons on the proposed rule change.

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

The NASD Regulation, Inc. (''NASD Regulation'') is proposing to amend Rule 11860 of the NASD's Uniform Practice Code to permit members to use the facilities of a Qualified Electronic Vendor for electronic confirmation and affirmation of depository eligible transactions. Below is the text of the proposed rule change (proposed new language is in italics; proposed deletions are in brackets):

11860. Acceptance and Settlement of COD Orders

(a) No member shall accept an order from a customer pursuant to an arrangement whereby payment for securities purchased or delivery of

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

securities sold is to be made to or by an agent of the customer unless all of the following procedures are followed:

(5) The facilities of a [securities depository] *Clearing Agency* shall be utilized for the [confirmation, acknowledgment and] book-entry settlement of all depository eligible transactions [covered by this Rule] except transactions that are to be settled outside the United States. *The facilities of either a Clearing Agency or a Qualified Vendor shall be utilized for the electronic confirmation and affirmation of all depository eligible transactions.*

(b) Definitions.

(1) *''Clearing Agency'' shall mean a clearing agency as defined in Section 3(a)(23) of the Act that is registered with the Commission pursuant to Section 17A(b)(2) of the Act or has obtained from the Commission an exemption from registration granted specifically to allow the clearing agency to provide confirmation and affirmation services.*

(2) ''Depository eligible transactions'' shall mean transactions in those securities for which confirmation, affirmation, [and] *or* book entry settlement can be performed through the facilities of a [securities depository] *Clearing Agency.*

[(2) ''Securities depository'' shall mean a clearing agency as defined in Section 3(a)(23) of the Act, that is registered with the Commission pursuant to Section 17A(b)(2).]

(3) ''Qualified Vendor'' shall mean a vendor or electronic confirmation and affirmation service that:

(A) Shall, for each transaction subject to this rule: (i) deliver a trade record to a Clearing Agency in the Clearing Agency's format; (ii) obtain a control number for the trade record from the Clearing Agency; (iii) cross-reference the control number to the confirmation and subsequent affirmation of the trade; and (iv) include the control number when delivering the affirmation of the trade to the Clearing Agency.

(B) Certifies (i) with respect to its electronic trade confirmation/affirmation system, that it has a capacity requirements evaluation and monitoring process that allows the vendor to formulate current and anticipated estimated capacity requirements; (ii) that its electronic trade confirmation/affirmation system has sufficient capacity to process the volume of data that it reasonably anticipates to be entered into its electronic trade confirmation/affirmation system during the upcoming year; (iii) that its electronic trade confirmation/affirmation system has formal contingency procedures, that the entity has followed a formal process of reviewing the likelihood of contingency occurrences, and that the contingency protocols are reviewed, tested and updated on a regular basis; (iv) that its electronic trade confirmation/affirmation system has a process for preventing, detecting, and controlling any potential or actual systems or computer operations failures, and its procedures designed to protect against security breaches are followed; and (v) that its current assets exceed its current liabilities by at least $500,000;

(C) When it begins providing such services, annually thereafter, and whenever it makes material changes to the services it provides, submits an Auditor's report to the Association and the Commission[2] *which is not deemed unacceptable by the Commission staff (for purposes of this subparagraph (C) ''material change'' means any changes to its systems that significantly affect or have the potential to significantly affect its electronic trade confirmation/affirmation systems, including: changes that: (i) affect or potentially affect the capacity or security of its electronic trade confirmation/affirmation system; (ii) rely on new or substantially different technology; or (iii) provide a new service to the Qualified Vendor's electronic trade confirmation/affirmation system); and*

(D) Immediately notifies the Association and the Commission in writing if it intends to cease providing services, and supplies supplemental information regarding their electronic trade confirmation/affirmation services as requested by the Association or the Commission.

(E) A vendor may cease to be qualified if the Commission staff: (i) deems the Auditor's report unacceptable either because it contains any findings of material weaknesses, or for other identified reasons; or (ii) notifies the vendor in writing that it is no longer qualified. If the vendor ceases to be qualified, the member using that vendor shall not be deemed in violation of this Rule if it ceases using such vendor promptly upon receiving notice that the vendor is no longer qualified.

(4) ''Auditor's report'' shall mean a written report that is prepared by competent, independent, external audit personnel in accordance with the standards of the American Institute of Certified Public Accountants and the Information Systems Audit and Control Association and that (i) verifies the certifications contained in subsection (b)(3)(B) above; (ii) contains a risk analysis of all aspects of the entity's information technology systems, including computer operations, telecommunications, data security, systems development, capacity planning and testing, and contingency planning and testing; and (iii) contains the written response of the entity's management to the information provided pursuant to (A) and (B).

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

In its filing with the Commission, NASD Regulation included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. 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) Background

NASD Uniform Practice Code (UPC) Rule 11860 was adopted in 1982 to resolve problems relating to the financial exposure to broker/dealers resulting from inaccurate and failed institutional transactions.[3] The financial exposure results from institutional customers that insist on ''COD/DVP'' transaction terms that permit them to delay payment for securities until the securities are delivered to the institution's custodian (the ''Cash-on-Delivery'') and to delay delivery of securities until payment is received (the ''Delivery-Versus-Payment'') (''customer-side'' settlement). Thus, unlike the terms of a retail transaction where payment and delivery to the clearinghouse are required within three days, the settlement occurs at the institution's custodian bank which does not make payment or release securities except in exchange for securities or payment.

Additional financial exposure occurs because the broker/dealer will usually sell or purchase securities on behalf of the institutional customer from another member (''street-side'' settlement). In

[2] With respect to the determination of whether a vendor is a ''Qualified Vendor,'' the Commission interprets NASD Regulation's use of the word ''Commission'' in the proposed rule change to mean Commission staff.

[3] Other SROs have adopted similar rules requiring confirmations/acknowledgments for institutional transactions to be processed through a registered clearing agency.

this situation, the member is subject to financial exposure for the institutional transaction until the institution's custodian bank forwards securities or payment that will cover the street-side transaction. The institution's custodian bank will only act on instructions in the form of an acknowledged confirmation.

Institutional transactions are large dollar transactions that require accurate communications among multiple parties to achieve settlement in numbers of accounts that the institution represents. If there is any delay in settlement with the institution or the transaction is a ''fail'' because the institution refuses to recognize the trade, the broker/dealer is subject to financial exposure for a large dollar, institutional transaction and subject to financing charges and additional net capital requirements during the time until settlement with the custodian bank or the member otherwise takes steps to clear the ''fail'' from its books.

The rules of the SROs were adopted jointly in 1982 to address the securities industry's inability at that time to process institutional securities transactions efficiently during periods of high-volume trading. Traditional manual methods of confirming, affirming, and settling such trades were costly, time-consuming, and prone to error, all of which led to an unacceptable number of failed transactions. The SROs sought to address these problems by requiring depository participants to use their depositories' automated systems for confirmation, acknowledgment, and settlement of depository-eligible trades. At that time the principal (and currently the only) confirmation/affirmation system operated by a depository was the Institutional Delivery (ID) system operated by the Depository Trust Company (DTC).

One vendor of institutional confirmation and acknowledgment services has expressed a desire to provide to DTC on behalf of their customers, confirmations and acknowledgments. Rule 11860, however, requires such providers to be registered clearing agencies. The vendor inquired about changing the rule to permit unregistered vendors to provide such services.

After discussions with various participants, users and regulators, NASD Regulation has developed a proposed rule change that will address the regulatory concerns involved in opening the clearance and settlement system to unregistered outside vendors, while at the same time exposing the process to the innovation and cost-cutting that competition from outside vendors can produce.[4]

(2) Proposed Rule Change

NASD Regulation is proposing to amend Subsection (a)(5) of Rule 11860 to permit either a Clearing Agency or a Qualified Vendor to provide electronic confirmation and affirmation of all depository eligible transactions. The principal provision of the proposed rule change is the definition of ''Qualified Vendor'' in proposed new subparagraph 10860(b)(3). The definition provisions address information formatting, vendor qualifications, vendor capability, and notice from the vendor of any changes to its services or systems. The provisions are designed to prevent and minimize disruptions in the clearance and settlement system that could result from participation by less-than-Qualified Vendors.

Under paragraph (b)(3)(A) of the proposed rule change a Qualified Vendor must be able to: (1) deliver a trade record to a Clearing Agency in the Clearing Agency's format; (2) obtain a control number for the trade record from the Clearing Agency; (3) cross-reference the control number to the confirmation and subsequent affirmation of the trade; and (4) include the control number when delivering the affirmation of the trade to the Clearing Agency. These requirements will ensure that the clearing agency's functions in completing the clearance and settlement of a transaction will not be disrupted by submissions from vendors that are incompatible with the clearing agency's systems.

Paragraph (b)(3)(B) of the proposed rule change requires a Qualified Vendor to certify that its electronic trade confirmation/affirmation system has a process for evaluating and monitoring capacity requirements. This process must permit the vendor to establish current and anticipated estimated capacity requirements. In addition the Qualified Vendor must certify that its system has sufficient capacity to process the data volume that it expects to handle. The Qualified Vendor also must certify that its system has formal contingency procedures that are regularly reviewed, tested and updated and that it can prevent, detect, and control systems or computer operations failures. The Qualified Vendor also must certify that it has followed a formal process of reviewing the likelihood of contingency occurrences. The Qualified Vendor also must certify that its procedures are designed to protect against security breaches and that the procedures are followed. Finally, a Qualified Vendor must certify that its current assets exceed its current liabilities by at least $500,000.

Paragraph (b)(3)(C) of the proposed rule change requires Qualified Vendors, when they begin to provide services, annually thereafter, and whenever they make ''material changes'' to their services to submit an ''Auditor's report'' to the Association and the Commission which the Commission staff does not deem unacceptable.[5]

In addition, for purposes of this subparagraph (b)(3)(C), the term ''material change'' means any change to its systems that significantly affect or have the potential to significantly affect its systems. Such changes include those that, affect or potentially affect the capacity or security of its electronic trade confirmation/affirmation system, rely on new or substantially different technology, or provide a new service to the Qualified Vendor's electronic trade confirmation/affirmation system. This notice provision is intended to prevent vendors from unilaterally and without notice upsetting the clearance and settlement system. Such advance notice will permit customers and regulators to evaluate the effect of the changes and take such steps as may be necessary to prevent disruptions in clearing and settling transactions.

Paragraph (b)(4) of the proposed rule change specifies that the Auditor's report is a written report prepared by competent, independent, external audit personnel in accordance with the standards of the American Institute of Certified Public Accountants and the Information Systems Audit and Control Association. The report must verify the vendor's certifications required under paragraph (b)(3)(B) of the proposed rule above. The report also must include a risk analysis of all aspects of the vendor's information technology systems, including computer operations, telecommunications, data security, systems development, capacity planning and testing, and contingency planning and testing. Finally, the report must include the vendor management's

[4] The Commission notes that the proposed rule change addresses the concerns raised by the Petition for Rulemaking filed by Thomson Financial Services (''Thomson'') with the Commission in December 1996. Thus, the Commission will respond to Thomson's petition after the final disposition of the proposed rule change.

[5] At this time, the Commission staff intends to indicate that a vendor's initial Auditor's report is not unacceptable and that the vendor therefore is a qualified vendor for purposes of Rule 11860 by issuing a letter to the vendor stating that it will not recommend enforcement action against any of the Association's member organizations that elect to use the confirmation/affirmation services of the vendor.

written response to the information provided under paragraph (b)(3)(A) and (B), above.

Paragaph (b)(3)(D) of the proposed rule requires Qualified Vendors to immediately notify the Association and the Commission in writing if they intend to cease providing services and supply supplemental information about their services upon the request of the Association or the Commission. This provision will provide the Association and the Commission notice of circumstances when vendors, in ceasing to provide services, may create disruptions to the clearance settlement system and to take such steps as may be necessary to minimize disruptions. In addition, this provision will permit the Association and the Commission to obtain information from vendors even though the vendors are not members of the Association or registered as clearing agencies. Such information is important to regulators in overseeing the clearance and settlement system.

Under paragraph (b)(3)(E) a vendor may cease to be qualified if the Commission staff deems the Auditor's report to be unacceptable either because it contains any findings of material weaknesses, or for other identified reasons, or notifies the vendor in writing that the Commission staff has determined that the vendor is no longer qualified. This provision will permit the Commission staff to evaluate whether a vendor is qualified at any time. The principal opportunities for the Commission staff to make such evaluations will be when the vendor submits its certifications and Auditor's report. In addition, the Commission will be afforded other opportunities to evaluate a vendor's qualifications through information obtained in connection with a vendor's notices under paragraph (b)(3)(D) or as a result of supplemental information supplied by a vendor under paragraph (b)(3)(E), or through information obtained from any other source available to the Commission. Finally, if a vendor ceases to be qualified, the member using the vendor must cease using the vendor promptly upon receiving notice that the vendor is no longer qualified. NASD Regulation is requesting that the proposed rule change be effective within 45 days of Commission approval.

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act[6] in that the proposed rule change will permit Qualified Vendors to offer confirmation, affirmation and related services in connection with the clearance and settlement of institutional securities transactions thereby increasing the options available to participants in institutional securities transactions and enhancing the clearance and settlement system.

(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

Written comments were neither solicited nor received.

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

Within thirty-five 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 ninety 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 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 in the Commission's Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing also will be available for inspection and copying at the principal office of NASD. All submissions should refer to File No. SR–NASD–98–20 and should be submitted by May 4, 1998.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

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[6] 15 U.S.C. 78o–3.

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39830; File No. SR–NYSE–98–07]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the New York Stock Exchange, Inc., Consisting of Amendments to Its Rule Regarding COD Orders

April 6, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] notice is hereby given that on February 18, 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, II and III below, which items have been prepared by the self-regulatory organization. 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

The proposed rule change consists of amendments to Exchange Rule 387 to permit electronic confirmation/affirmation of depository eligible COD Orders by ''Qualified Vendors.''[2]

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 self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

[2] The text of the amendments is attached as Exhibit A to this notice.